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Americans are fed up with George Bush's Republicans, but the Democrats still have a lot to prove: leader

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Politics this week

Apr 20th 2006
From The Economist print edition

The promised shake-up of White House staff began in earnest. **Scott McClellan**, the press secretary, announced his resignation and George Bush picked **Rob Portman**, the current United States Trade Representative, as his new budget chief (Susan Schwab, Mr Portman's deputy, is promoted to the top spot). In a surprise move, **Karl Rove** will lose some of the policy co-ordination duties he took on a year ago, but remains Mr Bush's deputy chief of staff. See article

Mr Bush and senior military personnel rallied around **Donald Rumsfeld** after several retired generals called for the defence secretary to resign over his handling of the occupation of Iraq. The Pentagon released a memo documenting the "unprecedented degree" to which Mr Rumsfeld consulted with senior officers. See article

AFP

George Ryan, a former Republican governor of **Illinois**, was found guilty of various federal charges linked to a corruption scandal involving bribes for trucking licences in the state.

Arizona's Democratic governor vetoed a state bill that would allow local authorities to arrest illegal immigrants and charge them with trespassing. Janet Napolitano, who said she had taken advice from the police, insisted the proposal was unworkable and blurred the line between state and federal responsibilities.

Thousands of people, including a dozen survivors, commemorated the 1906 **San Francisco** earthquake on April 18th at 5.12am, the exact time that the disaster struck. Around 3,000 people were killed in the quake, which destroyed vast tracts of the city.

Cocaine high

After several years in which it claimed that coca production in **Colombia** was falling swiftly, the United States found that it had increased by 26%, to 144,000 hectares (356,000 acres), after almost doubling the area surveyed. Since 2000, Washington has spent some $4 billion helping Colombia's government to fight the drug trade.

Venezuela's president, Hugo Chávez, announced that his country would withdraw from the five-country **Andean Community** because two other members, Colombia and Peru, had signed free-trade agreements with the United States.

Three ministers in **Bolivia's** leftist government were kidnapped by townspeople supporting foreign investment in their country. The ministers told residents of Puerto Suárez that a steelworks being built by a Brazilian firm broke a law barring foreign ownership near the borders. Security forces later released them.

Trade to the fore

EPA

Hu Jintao, **China's** president, made Seattle his first stop on his visit to the United States, before heading to Washington, DC, for a “formal lunch” with George Bush. See article

Australia dispatched 180 soldiers to the **Solomon Islands** after rioters wrecked its capital, Honiara, following an election. Australia already had several hundred police in the Solomons as part of a regional peacekeeping force.

Singapore called a parliamentary election for May 6th. Opposition leaders are hoping to contest at least half the seats, though another easy win by the ever-ruling People's Action Party seems certain. See article

Vietnam's ruling Communist Party began its tenth congress. Corruption was high on the agenda, following a scandal involving transport ministry officials.

A general strike and political demonstrations continued in **Nepal** against the king, paralysing the capital, Kathmandu. Tens of thousands defied government curfew zones, resulting in the deaths of several protesters. See article

President Gloria Macapagal Arroyo of the **Philippines** announced that she would commute to life imprisonment the death sentences of some 1,200 convicts on death row. Under a bill to be introduced to parliament, all future death sentences would likewise be commuted until the end of her term in 2010.

That Florida moment

The top appeals court in **Italy** confirmed a narrow victory for a centre-left coalition, led by Romano Prodi, over the outgoing government of prime minister Silvio Berlusconi in last week's bitterly contested general election. Parliament reconvenes on April 28th but a new government may not be constituted until June.

The **German** government, yielding to international pressure, finally agreed to open a huge collection of records relating to concentration camps and slave labour under the Nazi regime. The files contain information about more than 17m people who were imprisoned or enslaved.

Mikhail Khodorkovsky, the imprisoned former head of the **Russian** oil company, Yukos, has been attacked with a knife by a cellmate, according to lawyers for the ex-tycoon. An associate of the businessman said the attack would not have been possible “without an order from above”.

The governor of **Hungary's** central bank was accused by the ruling Socialist party of meddling after he criticised their fiscal record ahead of a second round of voting in parliamentary elections.

Intended to provoke

A suicide bomber from the West Bank, a member of Islamic Jihad, killed nine people in **Tel Aviv**. The Hamas government defended his action. Israel refrained from direct retaliation. Meanwhile, Jordan accused Hamas of smuggling arms into the kingdom and scouting targets there. See article

Muslims and Christian Copts battled in the **Egyptian** port city of Alexandria after a Copt was stabbed to death. See article

Nigeria's president, Olusegun Obasanjo, announced a new development plan to alleviate poverty in the oil-rich Niger delta region. Militant groups fighting for a larger share of oil revenues rejected the plan, and renewed their offensive, killing at least two people in an attack on an army barracks.

Kenyan MPs approved a report that implicates senior ministers and civil servants in corruption. Several other ministers have already resigned over the Anglo Leasing affair, and this latest move could lead to the prosecution of the vice-president, Moody Awori.

President Robert Mugabe said his opponents in **Zimbabwe** were “playing with fire” and threatened action if they organise against him. He also promised to extend state control over the mining industry.

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Business this week

Apr 20th 2006
From The Economist print edition

The **London Stock Exchange's** share price hit a new high (following last week's gains made after NASDAQ revealed it had become the LSE's biggest shareholder) as investors pondered the possibility of a takeover bid from the New York Stock Exchange. The speculation focused on a regulatory filing by the NYSE, which recently listed its own shares, confirming it was in merger talks with unnamed rival exchanges. See article

In a further sign of the increased competition among exchanges and the blurring of lines between asset classes, the **International Securities Exchange**, the biggest equities options exchange in the world, announced it was launching the ISE Stock Exchange with the backing of several Wall Street banks. It will be fully electronic and is expected to start operating later this year.

Standard Life revealed it had rejected several approaches from companies interested in a merger and is to press ahead with its planned demutualisation this summer. Europe's biggest mutual insurer said it expects to be valued at up to £5.5 billion ($9.8 billion) on its stockmarket debut, which is subject to a vote in May by its members.

Sandy bows out on a high

Citigroup, America's biggest financial-services company, reported a net profit of $5.6 billion for the first quarter on the back of strong performances from its international and investment-banking businesses. Citigroup released its statement shortly before Sandy Weill stepped down as chairman at a glitzy shareholders' event.

Kohlberg Kravis Roberts is to pay $850m for an 85% stake in the software-development and solutions unit of **Flextronics**, a company that makes products, including Microsoft's Xbox 360 gaming consoles, for the electronics industry. The unit is based in India (Flextronics is headquartered in Singapore) and KKR's is the biggest-ever leveraged buy-out by a private-equity firm operating in the country. See article

Tata Consultancy Services announced a further expansion that will result in an extra 30,500 people being employed by the company in the coming year. India's biggest exporter of software services, which also said net profit rose by 41% in the year ending March 31st, has benefited from a surge in outsourcing, most notably by big financial-services firms.

Down in the Valley

Intel reported poor earnings. The world's biggest chipmaker said net profit had fallen by 38% in the three months ending April 1st, compared with a year ago, to $1.35 billion. The company has been losing market share to Advanced Micro Devices, a Silicon Valley rival with which it is in fierce competition, and predicts a further fall in demand for its chips.

Wal-Mart is to stop stocking rifles and shotguns in a third of its shops in the United States (where it is the biggest seller of guns) because of a lack of demand. The decision should do no harm to the retailer's efforts to break into urban shopping locales, where it has sometimes met with stiff resistance.

Knight Ridder, which is America's second-biggest newspaper publisher and is being acquired by McClatchy, a smaller rival, said net income had fallen by 53% in the first quarter compared with a year ago. McClatchy is reportedly close to finding buyers for the 12 Knight Ridder titles it is selling.

BAA confirmed it had rejected a takeover approach by a consortium led by the ubiquitous Goldman Sachs that valued the operator of several British airports, including Heathrow, at £9.4 billion ($16.4 billion), around £650m higher than the hostile bid BAA is fighting from Grupo Ferrovial, a Spanish construction firm.

The **International Monetary Fund** released its latest semi-annual *World Economic Outlook* and raised its forecast for global GDP growth in 2006 to 4.9%. The fund also slightly raised its growth forecasts for the United States and the euro area (to 3.4% and 2.0% respectively), but expects China's GDP to grow by 9.5% this year, up from the forecast of 8.2% it made last September. See article

The price of **oil** reached record highs, pushing well past $70 a barrel. Fears that oil supplies might be jeopardised by any confrontation with Iran contributed to market jitters. See article

Losing some of its shine

Saudi Arabia's **Tadawul All Share index**, the biggest stockmarket of any Arab country, and a star performer in 2005, fell by 7.6% on April 18th, continuing a slide that has seen it fall by around 36% from its peak in February. Some analysts pointed to the suspension by Saudi regulators of two dealers on allegations of manipulating markets as one factor that has spooked wealthy investors.

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American politics

Taking on George Bush

Apr 20th 2006
From The Economist print edition

The Democrats still have a lot to prove

Getty Images

SNIFF the air in Washington, DC, this spring and you notice the smell of decay. The Republicans have been America's dominant party, winning seven of the past ten presidential elections and controlling both houses of Congress since 1994 (except for a brief interlude in 2001-02 when one of their senators defected). And their institutional power has been as nothing compared with their ideological clout. Wherever you look—from welfare reform to foreign policy—the conservative half of America has made all the running.

Yet this machine is stalling. The White House is doing its best to engage in some emergency repairs. The past few weeks have seen the appointment of a powerful new chief of staff, Josh Bolten, and a new director of the Office of Management and Budget, Rob Portman. Karl Rove, George Bush's chief political adviser, is also giving up his policymaking role to concentrate on preparing for this November's elections. But the party's problems go too deep for personnel changes to solve.

Mr Bush is the most unpopular Republican president since Richard Nixon: a recent *Washington Post*-ABC poll showed that 47% of voters “strongly” disapprove of his performance. Tom DeLay, the former House majority leader who did more than anybody else to build the conservative machine in Congress, is retiring in disgrace, the better to focus on his numerous legal problems. More Republicans may well be implicated in the Jack Abramoff lobbying scandal in the coming months.

The ideological shine has gone, too. The party of streamlined government has been gorging on legislative pork. A party that once prided itself on businesslike pragmatism has become

synonymous with ideologically skewed ineptitude of the sort epitomised by Donald Rumsfeld (see article). “What is the difference between the *Titanic* and the Republican Party?” goes one joke in conservative circles. “At least the *Titanic* wasn't trying to hit the iceberg.”

This presents an opportunity for America's other big party. The Democrats hope to win this year's congressional elections in November and, on the back of those, to capture the White House in 2008. They need a net gain of 15 seats to take over the House and six seats to take over the Senate.

With two-thirds of Americans convinced that their country is heading in the wrong direction, this might appear to be easy. It isn't. First, various technical factors—from the power of incumbency to gerrymandering—will help the Republicans in November. More important, if the Republicans reek of decay, the Democrats ooze dysfunctionality: divided, beholden to interest-groups and without a coherent policy on anything that matters to America and the world (see article).

It is never easy for America's out-of-government party. There is no leader of the opposition, and the cleverer presidential candidates may want to keep their powder dry till 2008. But it is not impossible to produce coherent ideas. In 1990 “New Democrats” began to gather round Al Gore and Bill Clinton; in 1994 Newt Gingrich rallied Republicans around his “Contract with America”. Nowadays “the alternative to Bush” is a muddle of vacuous populism and meaningless slogans (who is not for “real security”, whatever that is?). Worst of all, the Democrats are marching backwards.

Take the party's economic policies. Mr Clinton stood for free trade and (after some retraining) a balanced budget. In 1993, 102 House Democrats, less than half the total, voted for the North American Free-Trade Agreement. Last year, only 15 Democrats defied the unions to vote for a smaller trade bill, the Central American Free-Trade Agreement. In the usually wiser Senate, only 11 out of 44 Democrats supported the bill, and John Kerry and Hillary Clinton were not among them. As for the budget, the Democrats' main criticism of Mr Bush's splurge is that he has not spent enough.

This, sadly, is symptomatic. Some Democrats are trying to unpick Mr Clinton's welfare reforms. Despite the party's rhetoric about protecting the poor, it has blocked most serious attempts to improve the schools poor children are condemned to attend. As for national security, the party seems to be veering ever further to the Michael Mooreish left. Two years ago, Mr Kerry savaged Mr Bush over Iraq, but talked relatively responsibly about a gradual withdrawal. Now the call from many of the party's leaders is to bring the troops home now—and hang the consequences for the region.

Familiar vested interests are sometimes at work. The Democrats' relationship with the teachers' unions is just as crony-ridden as (and even more damaging to America's long-term interests than) the White House's ties to Big Oil. But there is also something new eating away at the Democratic brain: fury at Mr Bush. And though Bush-bashing may be understandable, it also looks increasingly counterproductive. The risk for the Democrats is that, although Mr Bush will retire to Crawford in 2009, he will have defined them as an anti-Bush party—isolationist because he was interventionist, anti-business because he was pro-business. Mr Rove would love that.

Incompetence v incoherence: the battle intensifies

Mention this to party activists and you will get the same complaint that Mr Clinton mercifully ignored in the early 1990s: you are just trying to turn their party into “Republican lite”. In fact, there are plenty of areas where liberal America needs to stand up bravely for its beliefs: against the death penalty, in defence of civil liberties, sounding a warning on global warming. American

voters respect principles and convictions; what they do not like is pandering to special interests and waffle.

The real danger facing the Democrats is that they become a permanent minority party—a coalition that enjoys support from the super-rich, a few minorities and the working poor, but is out of touch with the suburban middle class, not to mention America's broader interests. Such a party might sneak a victory this year, thanks to Mr Rumsfeld *et al*, but then get hammered by, say, John McCain in 2008.

Two years ago, this newspaper narrowly favoured Mr Kerry's incoherence over Mr Bush's incompetence (see article). Since then, Republican incompetence has exceeded even our worst fears. How depressing to report that Democratic incoherence has soared too. America deserves better.

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Iran, Israel and Palestine

Rejecting Israel, again

Apr 20th 2006
From The Economist print edition

The refusal to accept Israel's right to exist harms Palestinians too

AP

EVERY so often, unpopular Muslim regimes on the periphery of the Palestine conflict find it expedient to propose eliminating the Zionist entity. Since his election last year, Mahmoud Ahmadinejad, Iran's president and chief Holocaust denier, has become a leading exponent of this familiar ruse. His promise last week that Israel would soon be wiped from the pages of history in accordance with the prophecy of the late Ayatollah Khomeini was therefore neither especially new nor—till Iran acquires nuclear weapons—especially frightening. And, of course, even with a bomb, even Mr Ahmadinejad might think twice about launching a nuclear attack that could lead to Iran's own swift destruction.

What is more depressing is the rise of a similarly atavistic strain of Israel-destroying rhetoric among the Palestinians themselves. It took the Palestine Liberation Organisation until the late 1980s to abandon its self-defeating fantasy that it had the power and the right to wipe Israel off the map. Now the Palestinians are in danger of revisiting the same dead end.

Like many successful Islamist movements, Hamas combines strong ideology with a shrewd pragmatism. But winning January's Palestinian elections has been discombobulating (see article). Since then its leaders have broadcast a blizzard of crossed and mixed signals about whether they would be content with a state in the West Bank and Gaza instead of all historic Palestine, and for how long. Yet they still seem unable to accept the request of America, Europe, Russia and the United Nations to renounce terror and violence, accept Israel's right to exist and honour the Palestinians' previous international undertakings. Worse still, Hamas this week sent out an unambiguously wrong signal by justifying as “self defence” the deadly Passover suicide-bombing in Tel Aviv by a smaller pro-Iranian Palestinian group, Islamic Jihad.

Right now it is Israel that has the better claim to be defending itself. Islamic Jihad makes ceaseless attempts to mount suicide-bombings in Israel and, with other groups, has been firing rockets at Israeli towns ever since Israel evacuated the Gaza Strip last summer. Israel has killed many members of the rocket-launching teams—and, by accident, some innocent bystanders too. But the deliberate targeting of civilians is a war crime in anyone's book, and under the agreements which Hamas refuses to honour, the Palestinian Authority (PA) undertook to make an effort to stop such attacks. Its president, Mahmoud Abbas, rightly denounced the Tel Aviv atrocity.

By condoning the attack instead, Hamas will find it harder to win broad international acceptance. That may be a price it is willing to pay. As Western countries give the PA less, Russia, Iran and the Arab states may give more. Moreover, any attempt by Israel to force the collapse of Hamas's government is liable to fail. For all Israel's power in the territories, it should be prevented by its own scruples and world opinion from starving the Palestinians into reversing their democratic decision.

By the same token, however, Hamas's efforts to establish a free Palestine look doomed to fail unless it pays Israel the basic price of admission to talks: recognition of its right to exist and an end to terrorism. On present showing, Hamas's leaders are not willing to make that leap. It is to be hoped that they can still change their mind. If they think Israel's offer of a decent two-state solution is a bluff, let them call it. History suggests that although both sides suffer when there is deadlock in this miserable conflict, the Palestinians tend to suffer more.

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Corporate regulation

In search of better SOX

Apr 20th 2006
From The Economist print edition

What can be done to loosen America's burdensome post-Enron rules?

Landov

ONLY yesterday companies the world over flocked to America to list their shares. For bigger, more established firms, the razzmatazz of a listing on the New York Stock Exchange was the mark of blue-chip status. For younger firms, a NASDAQ listing was a crucial step on the way to becoming the next Microsoft. Today, however, foreign listings have become a rarity, especially on NASDAQ. Even some of America's home-grown would-be Microsofts now list not in New York, but overseas, especially on London's Alternative Investment Market.

It used to be taken for granted in the United States that the country's stockmarkets were the best-regulated in the world, and that their attraction to overseas companies was proof of the fact. So what does it mean that many of those firms now opting to list elsewhere pin much of the blame on the burden of America's corporate regulations—above all the Sarbanes-Oxley act (SOX) passed by Congress in 2002 after the scandalous collapse of Enron and WorldCom?

To its defenders, and there are still many, SOX has done just what was asked of it and raised the quality of corporate regulation so as to minimise the risk of the next Enron or WorldCom. If the price of that is for flakier Russian companies to choose laxer jurisdictions overseas, so much the better.

That argument might wash were SOX a well-crafted piece of legislation, rather than a rush-job hurried through a Congress with its eye on 2002's mid-term elections. SOX's sceptics are not restricted to fundamentalists who think that the legislation was always unnecessary or went after the wrong targets. Today, many people who supported SOX in principle—ranging from the boss of NASDAQ to the sainted former chairman of the Federal Reserve, Alan Greenspan—are increasingly disturbed by SOX in practice.

Strangled by red tape

How could SOX be improved? Divisions in Congress mean that thorough reform is unlikely anytime soon, even though some parts of the legislation could do with a second look. The priority is to modify the most hated part of SOX, the 20 lines of text called Section 404, which regulates the internal controls used by firms in their financial reporting and extends scrutinising to such minutiae as travel expenses and petty cash. The cost of implementing Section 404 has been far higher than expected, especially in smaller firms. Happily, several changes could lighten the burden of Section 404 and these can probably be seen through by America's main markets regulator, the Securities and Exchange Commission (SEC) without troubling Congress (see article).

A good start would be for the SEC to follow the likely advice of its own Advisory Committee on Smaller Public Companies and exempt companies with a stockmarket value below $128m and sales of less than $125m. That would still leave the bigger firms that account for 94% of the value of America's stockmarkets subject to Section 404. The SEC should also try to lighten the burden on them too. It could, for example, narrow the scope of the internal-control review carried out by auditors so that they examine only the larger risks, not the size of people's lunch expenses.

Small technical changes, perhaps, but in SOX, the detail is what costs the money. At the least such reforms would help restore the reputation of America's stockmarkets. They might even make America's own companies more competitive.

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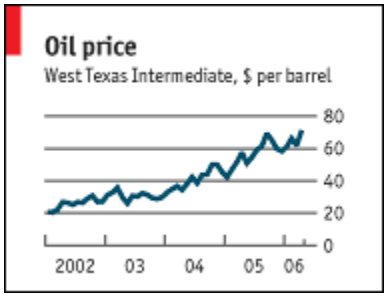
The oil market

Nostalgia for calmer days

Apr 20th 2006
From The Economist print edition

Uncertainty looks a bigger problem than high prices



HOW high can the oil price go? It is striking that so many people are even asking the question—let alone answering it, in some cases, with frightening triple-digit numbers. For most of the 1980s and 1990s, the oil price rarely strayed far from $20 a barrel. With the exception of a brief interlude following Iraq's invasion of Kuwait in 1990, the world grew used to the joys of cheap oil. But over the past four years, the price has more than tripled, to more than $70 a barrel. It is still climbing and prices in the futures market imply that oil will remain dear for several years to come. Clearly, investors believe that some comfortable old certainties have gone out of the window.

Chief among them is the idea that Saudi Arabia will always act to cap prices. The Saudis have many decades-worth of oil left in the ground, and so have an incentive to keep the stuff cheap enough to ward off conservation or substitution. To this end—and to help its protectors in Washington, DC—the kingdom used to maintain spare pumping capacity of a few million barrels a day, enough to deal with an unexpected surge in demand or a sudden cut in supply. During the first Gulf war, for example, Saudi Arabia turned on the taps to compensate for the loss of Iraq and Kuwait's normal output. But as demand has grown over the past few years, particularly from booming places like China, supply has not kept pace, so Saudi Arabia's buffer has gradually worn through. For the first time in more than two decades demand is straining at capacity.

A freer oil market is no bad thing. In time, higher prices will lead to conservation—a bonus in a world worried about global warming (though one better achieved through taxes). In addition, oil firms should respond to higher prices by redoubling their efforts to procure more of the stuff. And so they are: by one estimate, 15m barrels of new capacity should come onstream by 2010 (see article). Moreover, despite a lot of scaremongering, the geological evidence suggests that there is still plenty of black gold in the ground.

The hitch is that the most promising territory for exploration lies in unstable places such as the Middle East and Russia. What is more, the oil is controlled by state-owned firms, which often seem blind to the signals sent by the market. While the supply remains tight any political or meteorological hiccup in a producing country (and there always seems to be at least one) will resonate through the markets.

Three other factors will add to the uncertainty. The first is the flood of new speculative investment in commodities, especially oil. Speculators are thought to have put more than $100 billion into commodities markets in the past few years, helping to propel the price of oil ever higher. But this new hot money could quit the oil market in an instant, causing prices to plunge (and throwing the energy industry's investment plans into disarray).

The second unknown is how expensive oil will affect the world economy. Past surges in the oil price have led to rises in inflation and interest rates that have triggered recessions. This time might be different, partly because growing demand, rather than a reduction in supply, has underpinned the price rise. That means it has been steady and gradual, giving consumers more time to adjust. In addition, inflation remains low and oil exporters are supporting consumption in the United States, the biggest importer (see article). Dearer oil will eventually curb demand—but at what price, and at what cost to the world economy, nobody knows.

Making oil

In the long run, the biggest uncertainty is technology. Western oil firms are beginning to address their difficulty in finding oil by manufacturing fuel instead. Man-made fuels, such as ethanol derived from plants, or diesel conjured from coal and gas, hold out the promise of secure and almost unlimited supply. But with today's technology these are much more expensive to produce than oil pumped from the deserts of Arabia. Until that changes, the oil market is set for an unnerving period.

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China, America and human rights

The should-list to discuss with Mr Hu

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From The Economist print edition

America should not hesitate to press China over human rights

Reuters

IT'S easy to be mesmerised by China: the double-digit growth, the ambitious space programme, the shining new cities along its teeming shore, the prospect of selling to the largest and one day perhaps the richest market on earth. And it is equally natural, too, to try everything from flattery to threats in the hope of enlisting its leaders as partners in the struggles with terrorism, nuclear proliferation, people-smuggling, carbon emissions and spiralling macroeconomic imbalances. Both these temptations will have been much in the minds of America's policymakers this week, as they welcomed China's president, Hu Jintao, to Washington, DC. But there is a danger here. The wish-list of things America wants China to do for America's sake has become so long that the “should-list” of things America should ask China to do for the sake of the Chinese people no longer gets serious attention at all.

The should-list has only one big item: China should abide by the Universal Declaration of Human Rights, much of which is echoed in its own constitution. At present it doesn't. It is true that in many ways, life in China has become freer: the state interferes far less in people's personal and economic lives than it used to. Speech and the press are less controlled than they once were. Yet China remains a deeply authoritarian state, brooking no possibility of organised opposition to the Communist Party. Media control, having relaxed over many years, is now tightening under Mr Hu. Experiments with allowing a free vote (for individuals, not for opposition parties) in local elections have remained just that. The judicial system is a travesty, with alleged wrongdoers sometimes held for months or years without charge. Less than half of one per cent of convictions are overturned on appeal. Beatings in custody with sticks and electric batons remain widespread, according to the UN. Human-rights groups say at least 50 people are still in prison because of their involvement in the peaceful Tiananmen demonstrations of 17 years ago. In 2004 an official said some 10,000 people are executed in China each year. And, of course, in China's recent acquisitions, Tibet and Xinjiang, repression is far worse than in the Han areas. All this is as much

part of China today as are the nightclubs of Shanghai's Bund.

It is sometimes argued that there is little America can nowadays do to promote human rights in China. After all, in 2000 it surrendered the single most effective lever it had when it ended the requirement for an annual review of China's most-favoured-nation trading status, a regular occasion for scrutiny and pressure. A year later, another lever was lost when Beijing's bid to host the 2008 Olympic Games succeeded. On top of this, many would add, its own abuses at Guantánamo and Abu Ghraib have robbed America of whatever moral authority it once had to lecture others on human rights.

Both arguments are misplaced. America still has a hold of sorts over China. Mr Hu craves respectability: he wants very much for a rising China to be treated as an equal, respected member of the world community. The West can make it clear that, for all its friendly intentions towards China, full acceptance will not come until China takes human rights seriously. As for Guantánamo and Abu Ghraib, these were indeed dreadful unAmerican aberrations for which America should make amends. But they are mistakes that would hurt human rights twice over if they deterred the United States from continuing to speak up for freedom and dignity in every country—however potentially powerful or lucrative it might be.

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Financial reform

Reality check at the IMF

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The fund needs a gentle overhaul, not a fundamental rethink

THE International Monetary Fund cannot seem to win. Every financial crisis is the cue for the world's economic Pooh-Bahs to declare that the organisation desperately needs reform. This year there is a conspicuous lack of crises, and yet, as they prepare for the IMF's spring meetings this weekend, the great and the good are at it again. Mervyn King, governor of the Bank of England, says the fund's role is obscure. Tim Adams, the main international man at America's Treasury, has accused it of being “asleep at the wheel”. Critics warn that the IMF faces irrelevance unless it reinvents itself radically.

That seems an extraordinary assertion. Less than a decade ago the world was rocked by emerging-market financial crises in which the fund was called on to save the day. Thanks to today's abundant liquidity, emerging economies have enjoyed easy access to private capital and hence no need for the IMF. But no one expects such liquidity to last forever. A temporary lack of fires does not remove the need for a fire brigade.

So what is really prompting the calls for reform? One disreputable reason to change is the internal workings of the IMF's budget. Bizarrely, the IMF makes money to pay for its staff only when it lends to countries in crisis. The lack of recent crises means the organisation faces a 30% drop in its income over the next two years. That suggests the IMF needs a new source of money, not a new role.

On two counts, however, the critics have a point. On the world's most intractable macroeconomic challenge, unwinding the imbalances between excessive borrowing in America and excess saving elsewhere, the IMF has almost no clout. Worse, many of the fund's potential clients in the

emerging world are the most excessive savers. They are doing their best to ensure that they never have to turn to the IMF again, by building up enormous foreign-exchange reserves, a hugely expensive and inefficient use of their resources (see article).

Most financial bigwigs think the fund's future lies in helping to sort out the big global imbalances. Mr King wants the IMF to follow Keynes's dictum and offer “ruthless truth-telling” when countries are going wrong. Endless proposals offer advice on improving “multilateral surveillance” and on making the IMF's board more independent.

Sadly, the fund's ability to tell rich countries what to do is extremely limited. Rich countries have not borrowed from the IMF in decades and will be deaf to the fund's wise words unless it suits their own domestic interests. Only if the fund had the ability to punish non-borrowing members (as, in theory, it did in 1944), would the focus on “surveillance” amount to much. But no rich country will give the IMF that power. It is naive to believe the fund can become a global financial guardian.

The IMF's future—rather like its recent past—lies with emerging markets, where access to international capital is more precarious than you might think. Should global financial conditions become less forgiving, many countries—whether Indonesia, Hungary or even Brazil—might once again need access to the IMF's cash. Even the strongest would be better pooling risks within the IMF than going it alone by building up huge independent reserves.

For that to happen, emerging economies must believe the IMF represents them. This calls for a shift of power away from Europe. It is absurd that Brazil, China and India have 20% less clout within the fund than the Netherlands, Belgium and Italy, although the emerging economies are four times the size of the European ones, once you adjust for currency differences. Emerging countries are keen to contribute more cash (and thus get more votes), and they have the support of Rodrigo de Rato, the IMF's Spanish boss. The Europeans, too, should support this reform. A smaller voice in a useful organisation is better than power over a moribund one.

An IMFurance policy

With more sway over the fund, emerging economies could shift the organisation's priorities. One sensible idea, recently raised by the IMF's chief economist, would be to pool some of their reserves in the IMF, in effect, using it as an insurance facility that offers rapid access to cash if strong economies are hit by financial turbulence. Some rich countries worry about the perverse incentives that would create. It is a dilemma: the risk is real, but so is the cost of a crisis. If many of the fund's clients want such a scheme, rich countries should not block it.

Doubtless, the agitators want much more. But, unlike their grand ideas, giving emerging markets a bigger voice and useful products would at least make the IMF more useful.

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New media

Talking to yourself

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Do not be too afraid of the coming age of mass participation

AP

FOR the past few weeks the “mainstream media” in America have been busy chewing over the choice of Katie Couric, a popular host of NBC's Today show, to become the anchor of the CBS Evening News in September. Those in other countries, as well as Americans under 30, may be forgiven for thinking that a news story about a newscaster is just a spectacular bout of navel-gazing. Of course it is—which is precisely why it holds a couple of lessons about “new media”.

News about News is partly the product of journalists' urge to talk about themselves—a pretty universal urge, as it turns out. The same impulse is the key to the changes sweeping through news and entertainment, as our survey on New Media describes. Mass media used to be one-way traffic from media to audiences. Readers, listeners and viewers, as a murmur besides the pontification of professionals, were consigned to call-in shows and the letters pages.

The shift to an era of participation challenges this. The infrastructure for delivering media content—the internet—is fast becoming ubiquitous. Ordinary people are creating their own blogs, wikis and podcasts, because it costs almost nothing to do so. Most of them do not care how large their “audience” is. Some choose to keep it small and intimate; a tiny number become stars—one-man and one-woman news organisations in their own right. Since the audience is made up of people who are themselves sounding off, new media are more of a hubbub than a homily.

Which leads to the second item on the Evening News: anxiety. Ms Couric's job matters because it is an attempt to shore up a crumbling institution. Media executives are not the only ones to fret as audiences decline. The CBS Evening News was first broadcast in 1948 and people are sentimental about the media they grew up with. The fear is partly about what might be lost from the mainstream, partly of what might replace it. Many fear that a cacophony leads to a splintered

society. How can anything good come from the clamour of so many raised voices? Isn't it an echo chamber in which those full of passionate intensity spend long hours sharing prejudices?

That is wildly pessimistic. For a start, in the age of mass participation, new media will co-exist with old—indeed it is already increasingly hard to tell when one becomes the other. True, ever more people will upload short video clips to new websites such as YouTube.com, go to Netflix.com to rate their DVDs, to Amazon.com to discuss books and their own blogs for online debate. But that will not replace Steven Spielberg's blockbusters or the *New York Times*'s network of reporters.

Moreover, the ease with which the internet spreads wrong-headedness—to say nothing of lies and slander—is offset by the ease with which it spreads insights and ideas. To regret the glorious fecundity of new media is to choose the hushed reverence of the cathedral over the din of the bazaar.

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On Thailand, Charles Taylor, immigration, the European Union, climate change, honours, Ayn Rand

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Thaksin's legacy

SIR – Your leader on Thaksin Shinawatra's resignation as prime minister of Thailand made some good points, but it is wrong to think that he has "genuinely helped" the rural poor ("A blow to Thai democracy", April 8th). This is a premature judgment. His rural-development policies may appear attractive on the surface, but dig deeper and you find a health-care system close to bankruptcy and a raft of government-backed loans that ignore the essential lessons of microlending. While buying motorcycles and mobile phones shored up his political base, and certainly helped "pump up domestic demand", it did nothing to tackle the rising debt in the countryside.

With interest rates rising and the economy slowing, debt will now become a major problem. It would have been better for Thailand if Mr Thaksin's ill-advised and self-serving grassroots policies played themselves out, which would have eventually turned his supporters away from him. The worry is that his resignation will spur the countryside to blame his successor when the inevitable destruction comes to pass, allowing him to return again in his ersatz role as "saviour".

H.P. Boothe
Taling Chan, Thailand

SIR – You raised the issue of whether dissenting protesters can harm an infant democracy. Those who demonstrated against Mr Thaksin have a legal right to protest peacefully. And opposition parties have a right not to contest an election, if that is how they want to object. Mr Thaksin's exit from politics (temporary though it may be) is actually a victory for Thai democracy.

Burapa Atthakor
Bangkok

SIR – I was surprised at your illiberal dismissal and scorn for "people power". Do you really question the right of people to demonstrate against their government? No government, even an elected one, has unlimited legitimacy. A democracy is measured not just by elections, but through the responsiveness of a government to people's rights and demands. You should have celebrated the non-violent discipline of the protesters instead of criticising the very technique of non-violent action, which is so crucial for enhancing and preserving democracy around the world.

Arthur Edelstein
Hayward, California

SIR – The cover of your Asia edition insinuated a violent and ugly mob, which is malicious considering the protesters in Bangkok were peaceful. They were the true supporters of democracy, demonstrating against the recklessly arrogant Mr Thaksin who turned Thailand into a demockerycy.

Frank Moore
Hua Hin, Thailand

Less of a drama

SIR – You say that Charles Taylor was "whisked through streets of cheering crowds" when he was brought to Sierra Leone to face charges of war crimes ("A big man in a small cell", April 8th). I was present at the compound of the Special Court of Sierra Leone at the time of Mr Taylor's arrival, and I must inform you that he was brought directly to the compound by helicopter. Crowds may have cheered, but he was not whisked through the streets.

Birgitte Vestberg
Special International Crimes Office of the Danish Prosecution Service
Copenhagen

Worker ethics

SIR – You made sound recommendations on immigration policy in the United States ("Sense, not Sensenbrenner", April 1st). I am the son of former "illegal aliens" from Mexico and a graduate of Harvard, and I support a comprehensive approach to the problem. But a more fundamental solution would be to eliminate the welfare state for natives and immigrants alike. Tear down the fences and let the free market regulate the flow of labour. Immigration levels, along with a market wage for labour, will reach equilibrium when all willing employers are matched to their willing workers. This would make clear what I have known my entire life—that the principal magnet for immigrants is work, not social services, and that the principal motivation for nativists is raw xenophobia, not economic considerations.

Jack Guerrero
London

Polling evidence

SIR – Charlemagne offers the contradiction that there is no proof that most EU nationals oppose enlargement when his case rests upon contrary opinion polling in the big six EU countries, accounting for 75% of the EU's population (April 1st). It would have been simply enough to reiterate that the results of the French and Dutch referendums on the European constitution provided no clear evidence against enlargement, given the diversity of strong concerns among voters about their respective governments' own domestic policies.

Ali M. El-Agraa
Professor, Faculty of Commerce
Fukuoka University
Fukuoka, Japan

Talking about the weather

SIR – Your analysis of the failings in British policy on climate change misses one key point ("Hot under the collar", April 1st). The instability of the global climate is a risk that requires a global

response and that process is being held back by concerns about the cost of mitigation. The catalyst for a more ambitious response will be proof from a major economy that you can “green and grow”. With a platform created by the dash for gas in the 1990s, Britain was well placed to make that crucial case. With emissions on the rise since 1997, we are letting that opportunity slip. That is the real cost of our failure to deliver on the rhetoric.

Nick Hurd, MP
House of Commons
London

SIR – Britain's policy places the burden of emission reductions almost exclusively on the power industry while allowing other industries, such as iron and steel, to increase theirs. This may be more politically palatable, but its efficacy is questionable. It is no surprise that such a one-sided policy is unsuccessful.

Stephen Emmert
Seattle

The new creditocracy

SIR – Napoleon is alleged to have remarked, when instituting the Légion d'Honneur, that “it is by such baubles that men are led” (“Going, going, gong”, March 25th). Would it not now be appropriate for Tony Blair to institute a new award called the Order of Dodgy Loans, thus not only encouraging transparency but ensuring his legacy?

Michael Thomson
Trouville, France

A fan of Ayn

SIR – Davide Mozza misses the point of Ayn Rand's objectivism (Letters, April 8th). He equates the argument that we should be able to sell our vital organs with being able to sell our daughters for dates. But unlike a daughter, an organ has no rights. And writing from Pisa he should know that the Italians have the best-looking women of any of us, so any male without a date there suffers voluntarily.

Alan Raye
Jacksonville, Florida

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America's Democrats

Happy days are here again—or are they?

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From The Economist print edition

Americans are fed up with George Bush's Republicans. But the Democrats look far from invincible

A CARTOONIST tells it best. An elephant lies snoozing. Sensing the time is right, a crowd of Democratic mice surround it and move in for the kill. “What's the plan?” asks one. “Plan?” asks another. “Maybe we should have a meeting,” says a third. “What if we win?” frets a fourth.

The Republicans are so unpopular that any semi-competent opposition party should be sauntering to victory in the mid-term elections in November. Only 36% of Americans think George Bush is doing a good job as president. Even Republican states are lukewarm: his approval rating is above 50% only in Idaho, Nebraska, Utah and Wyoming. And Americans like the Republican-led Congress even less: a paltry 23% of them approve of its performance.

With America mired in Iraq and the Republicans mired in scandal, the Democrats have plenty of large, slow-moving targets to aim at. When they accuse Mr Bush of valuing loyalty above competence, he obligingly refuses to sack Donald Rumsfeld, the bungler-in-chief in Iraq. When they decry the ruling party's “culture of corruption”, people think of Randy “Duke” Cunningham, a bribe-trousering ex-congressman whose marble-topped commode was among many ill-gotten items the FBI auctioned last month.

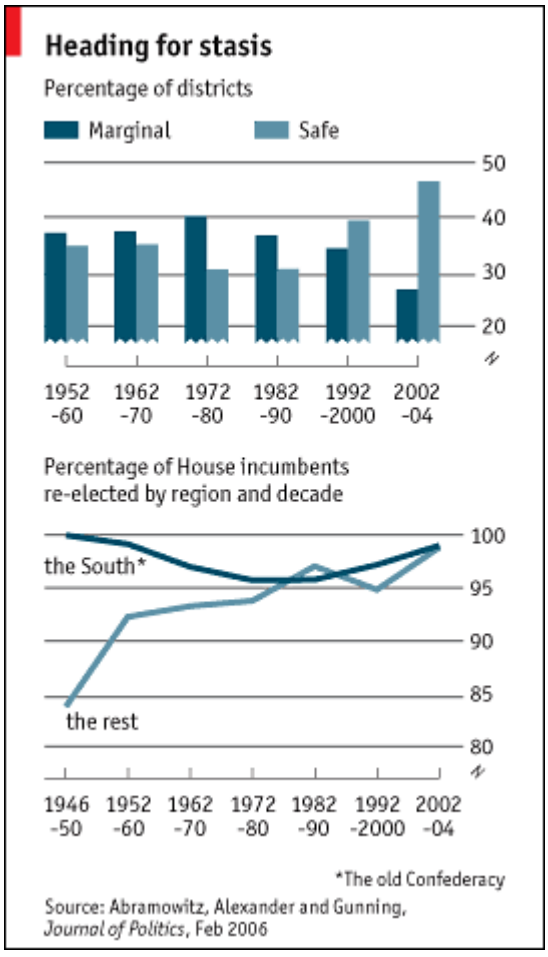
Yet Pat Oliphant, the cartoonist who drew the muddled mice, is not the only one to doubt the potency of the Democrats. “For the Americans in the middle, who have no strong partisan allegiances, we have failed to articulate a real plan or vision,” say Markos Moulitsas Zúniga and

Jerome Armstrong, two of the most popular Democratic bloggers. “It's not that people know what we stand for and disagree; it's that they have no idea what we stand for,” say James Carville and Paul Begala, two of the architects of Bill Clinton's winning presidential campaign in 1992. The junior senator from Illinois, Barack Obama, one of the Democrats' most admired politicians, has tried to make a joke of it. “You hear this constant refrain from our critics that Democrats don't stand for anything,” he remarked the other day. “That's really unfair. We do stand for anything.”

In fact, both parties are a tangle of contradictions. But whereas the Republicans have one clear leader—the president—the Democrats do not. Should voters pay more attention to Nancy Pelosi, their leader in the House of Representatives, Harry Reid, the top Democrat in the Senate, or one of the scrum of Democratic presidential hopefuls? And since the Democrats control no branch of the federal government, their national record of late is one of speeches and protest votes, rather than actions whose merits can be judged. All this makes it hard to predict what might happen were they to win back one or both houses of Congress in November.

A Democratic takeover is far from assured. Granted, they have a double-digit lead in the polls. In a survey by AP-Ipsos this month, 49% of respondents said they would rather the Democrats ran Congress, whereas only 33% preferred the Republicans. But polls are unreliable. Not everyone who grumbles about Mr Bush will vote: turnout in mid-term elections is typically not much more than a third. And other obstacles must be overcome.

In the House, all 435 seats are up for election, but incumbents seldom lose these days. Southern seats—those in the 11 states of the old Confederacy—became more competitive in the 1980s, but have since joined the trend elsewhere (see charts). Nowadays, no matter where they are, over 90% of those who run tend to be re-elected (98% in 2004), thanks to gerrymandering and the ease with which those in power can raise money. The Senate is unsullied by gerrymandering, since state borders cannot be redrawn. But only a third of the Senate's seats are up for election, and sitting senators are even better at raising money than incumbents in the House. In the current campaign, the Republicans have so far raised $321m and the Democrats $226m.



The Democrats need to win 15 extra seats to capture the House and six to take the Senate. The last time such a revolution hit Capitol Hill was in 1994, when the Republicans seized both Houses. That victory came partly because voters were fed up with a Democratic Party that had grown complacent after too long in office, much like today's Republicans. But it was also because Newt Gingrich and his cohorts offered a clear platform: the tax-slashing, government-shrinking “Contract with America”. The Democrats have no manifesto to compare with this, but they have been trying, in recent weeks, to give voters some idea of where they stand.

The Mommy party girds for battle

Their weakest issue has long been national security. On Iraq, the Democrats are tarred by

association with the loopier critics of the war in Iraq, and by outbursts of defeatism among their own leaders. Howard Dean, the party chairman, said last year that the “idea that we're going to win the war in Iraq is an idea which is just plain wrong.” As for the broader fight against terrorism, Democrats often sound as though they do not take it as seriously as other Americans. Moreover, Democratic activists are obsessed with the idea of impeaching Mr Bush. His alleged offence is to have ordered warrantless wiretaps to catch terrorists when, many lawyers argue, warrants were required. The party leaders do not want to make this a campaign issue, because Republicans would then say Democrats cared more about terrorists' privacy than American lives.

To combat the charge that they have a “pre-9/11 world view”, Democratic leaders have done their best to recruit ex-servicemen to run for the party. And last month the top two Democrats in Congress, Mr Reid and Ms Pelosi, surrounded themselves with fire-fighters, police and veterans to unveil a strategy for “Real Security”. This document would be more convincing as a call to arms if it did not read like a string of phrases chosen for their popularity with focus-groups and then crammed into one sentence after another. For example: “To Ensure Unparalleled Military Strength and Honour our Troops, we will rebuild a state-of-the-art military by making the needed investments in equipment and manpower so that we can project power to protect America wherever and whenever necessary.”

Churchillian it may not be, but most of “Real Security” is sensible. The trouble is that its main hard proposals—kill Osama bin Laden, train more special forces, reduce dependence on Middle Eastern oil and make 2006 “a year of significant transition to full Iraqi sovereignty”—sound awfully similar to Mr Bush's plans.

Where the details differ, the Democrats' suggestions are sometimes footling (create “a national tyre fuel-efficiency programme”) or daft (criminal penalties for energy companies that “price-gouge”). One throwaway commitment casually promises to reshape the world: the Democrats would “[e]liminate terrorist breeding-grounds by combating the economic, social and political conditions that allow extremism to thrive.”

To be fair, it is difficult to produce a national-security platform that amounts to much in a year when the presidency is not being contested. Even if the Democrats win both houses of Congress, Mr Bush will remain commander-in-chief. In the end, the national-security debate boils down to this. Voters doubt that the Democrats take terrorism as seriously as the Republicans do, but they also doubt that the Democrats could be as incompetent in fighting it. One recent poll showed that the Republicans' long-standing advantage as the party people trust to protect America had dwindled to nothing. That should scare the party of Dwight Eisenhower, Ronald Reagan and George Bush senior.

On most other issues, people tell pollsters that they prefer the Democrats. On the economy, there are some good reasons to do so—though tempered by doubts. America's most urgent macroeconomic ill is the federal government's budget. Under Mr Bush, this has slithered from showing a surplus of $236 billion in 2000 to running a deficit of $318 billion in 2005. That would be worrying enough in normal circumstances, but with the baby-boom generation about to retire and start claiming Social Security (government pensions) and Medicare (government health care for the elderly), it heralds catastrophe.

The Democrats are trying hard to sound fierce about the deficit. Hillary Clinton, their most prominent presidential aspirant, declared recently that “red-ink fiscal policies will undermine America's competitiveness”. The party promises to restore the “pay-as-you-go” principle that was scrapped in 2002. In other words, all new tax cuts or spending would have to be balanced by new savings. But do the Democrats propose any specific tax increases or spending cuts that might actually bridge the deficit? Apart from promising to repeal Mr Bush's tax cuts for “the rich”—whom they take care not to define too clearly—no. In opposition, anyway, they have clamoured above all

for more spending.

All cheques, no balances

The two strongest reasons for thinking that voting Democratic might improve fiscal discipline have nothing to do with the Democrats' campaign promises. One is that the Republicans have been so profligate. The other is that divided government would give both parties a scapegoat. If Mr Bush had to share power, he could blame the Democrats for everything that hurt his supporters, and they could blame him for everything that hurt theirs. That way, something might be done.

But in truth, neither party has a serious plan for grappling with the long-term shortfall that will be caused by the baby-boomers' retirement. Economists close to the Democratic Party understand the problem. In a recent paper for the Brookings Institution, a Washington think-tank, Alan Auerbach, William Gale and Peter Orszag predict that the boomers' demand for doctors, drugs and pensions will help inflate the federal budget deficit to a crippling 10.8% of GDP. But, they sigh, “Dealing with these imbalances will require spending cuts or tax increases that are far beyond the scale of anything currently considered politically palatable.”

One topic on which the Democrats are plainly less liberal than the Republicans is trade. Bill Clinton may have had the courage to push through the North American Free-Trade Agreement in 1993, but his party is now increasingly protectionist. Mrs Clinton describes herself as “a very staunch supporter” of trade agreements, but voted against the Central American Free-Trade Agreement last year, and also against granting the president clear authority to negotiate such deals. Only 25% of Senate Democrats backed the Central American one, and only 15 out of 202 Democrats in the House.

Party leaders deny that they are protectionist. They prefer to say they support “fair trade”. That is, they want to impose rich-world labour standards on countries whose competitive advantage is low labour costs. This is old-fashioned protectionism masquerading as compassion. If “fair trade” became American policy, the results would be higher prices for American consumers and higher unemployment in the rest of the world.

Some Democrats argue that if support for globalisation is to be maintained, more must be done to ease the plight of those who are hurt by it. Fair enough, but they would sound more convincing on this if they did not also shamelessly scaremonger about China, outsourcing abroad and the prospect of Arabs running American ports. A Democrat-controlled Congress would pose a grave threat to the further liberalisation of world trade—and so to world prosperity—unless power prompted the party to become more responsible.

Issue by issue

On microeconomic issues, the Democrats offer a grab-bag of policies. They want to raise the minimum wage. They would extend Medicaid (health insurance for the poor) to include more, slightly-better-off people. They would offer a tax credit to help small firms and the self-employed with their health costs. They would let all 55-65-year-olds buy their health insurance from Medicare. They would subsidise saving for retirement by up to $1,000 a person for 100m less-well-off Americans.

Taken as a whole, the party's various economic manifestos sound cautious but fairly expensive. More eye-catching ideas can be found among the party's independent advisers. The Hamilton Project, for example, has a new idea for schools. Since studies suggest that the current system of

teacher certification is worse than useless (it puts off clever would-be teachers), the Hamiltonians propose that schools should ignore it and simply hire teachers with good academic qualifications, whose teaching ability would then be assessed after two years. This has worked in Los Angeles. The teachers' unions would surely oppose it. By embracing it, the Democrats would show they can stand up to one of their own interest-groups.

In “Crashing the Gate”, Mr Armstrong and Mr Moulitsas complain that

> single-issue groups not only hurt the Democratic Party in its search for a common identity, but they help provide the Republicans with a treasure trove of attack opportunities. While the Democratic Party should be the party of people, it has become, with a lot of help from Republican framing, a party of “immoral” abortionists, “extremist” tree-huggers, “corrupt” labour officials, “greedy” trial lawyers, “predatory” homosexuals and “anti-white” minority activists. After all, these are the loudest and most influential voices in our party...so it's not a stretch for demagogic Republicans to paint Democrats as a loose collection of selfish people who are fanatical about their specific cause and have no larger concerns—for the economy, the military, or the country.

This is a shrewd analysis. The Republicans have a crackpot fringe, too, but the Democratic Party often sounds as though it consists of little else. Democrats seeking public office are besieged by single-issue groups urging them to adopt policies that most Americans disagree with, such as support for racial quotas and unrestricted late-term abortion.

Some Democratic politicians simply say no. Brian Schweitzer won the governorship of Montana in part because he binned all the questionnaires that single-issue groups sent him to complete. All but one—the form from the National Rifle Association. “You've got to fill that one out,” he told Mr Armstrong and Mr Moulitsas. “In order to get an ‘A-plus’, you've got to shoot somebody.”

Mr Schweitzer is an exception, however. Many more Democratic politicians have, over the past 30 years, tried to duck controversial moral issues by leaving them to the courts. Judges have stepped into the legislative vacuum, often infuriating conservatives and making Democrats sound ridiculous. In January, for example, during the confirmation hearings for Samuel Alito, Mr Bush's latest choice for the Supreme Court, some Democratic senators upbraided the judge for wanting to apply the law, not make it. Surely it would be better, “to ensure social progress”, if judges took “a more expansive, imaginative view of the constitution?” wheedled Senator Herb Kohl of Wisconsin. In other words, Mr Kohl, a legislator, wants judges to do his job for him. This is how abortion was legalised in America, how prayer was barred in schools and how gay marriage came to Massachusetts.

Another group with whom the party has stormy relations is typified by Mr Moulitsas, whose website, DailyKos.com, is the meeting-place for hundreds of thousands of people who hate Mr Bush. Online activists, or “netroots”, as they call themselves, raise lots of money and provide lots of publicity for Democrats. Since Mr Dean's bid for the presidential nomination in 2004, which was buoyed by large numbers of small donations raised online, party elders have paid respectful attention to young lefty bloggers. Mr Reid, the Senate minority leader, has agreed to speak at the *Daily Kos* convention in June. Mark Warner, one of Mrs Clinton's rivals for the presidential nomination in 2008, employs Mr Armstrong as an adviser.

The embrace is awkward, though, because the netroots are always goading the party to get as angry as they are. They tend to favour the most frothingly anti-war, Bush-bashing candidates, who usually lose at the polls. And they express themselves in terms both crude and petulant. Four-letter words and wishes for Mr Bush's slow death are common on left-wing blogs.

Somehow, the Democrats must harness their activists' rage without themselves sounding unelectably shrill. And it would help if they offered voters some bold, purposeful reasons to back them. Their current platform is not, as Newt Gingrich put it, a mere “Contract with San Francisco and Vermont”. But neither is it a compelling vision of America's future. That said, it may be enough to win in November. After looking at the latest opinion surveys, a Republican pollster called Tony Fabrizio said: “The good news is Democrats don't have much of a plan. The bad news is they may not need one.”

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The president's economic team

Where to on trade?

Apr 20th 2006 | WASHINGTON, DC
From The Economist print edition

AFP

What George Bush's reshuffle implies about his economic strategy

OVER on the west coast, China's president, Hu Jintao, was touring Boeing's factory and dining with Bill Gates. As *The Economist* went to press, Mr Hu's long awaited trip was to take him on to Washington for a formal lunch (though, pointedly, not a state dinner) with George Bush. Trade was high on the agenda. But Mr Hu was making for a town where Marine One was stubbornly refusing to leave the White House lawn, and where trade policy too seemed in a bit of a fix.

On the advice of Josh Bolten, the new chief of staff, Mr Bush has begun to reshuffle his White House team. The president's spokesman, Scott McClellan, has left, and the job of Karl Rove, his chief policy advisor, has been altered (see article). But the most important change, in terms of economic policy and relations with China, is the shift of Rob Portman, Mr Bush's top trade negotiator, to head the Office of Management and Budget, which oversees the $2.8 trillion federal budget.

What does this mean? One obvious conclusion is that Mr Bush has scaled back his ambitions for freer trade, either in the multilateral Doha round or in the plethora of bilateral trade deals that America is negotiating. Mr Portman's political stature and connections on Capitol Hill (he was previously a member of the House) showed that the Bush team was determined to get trade deals through Congress. Although his successor, Susan Schwab, currently Mr Portman's deputy, is a competent trade lawyer with plenty of congressional experience, she does not have her predecessor's political heft.

That the White House sees little need for a heavyweight in the trade job suggests it is sceptical about the Doha round, reluctant to push controversial bilateral deals and in no mood to try to convince Congress to extend the Trade Promotion Authority, which expires in June 2007. All this is a blow for freer global trade, but the decision is neither surprising nor unjustified. Despite Mr Portman's efforts, the Doha round is virtually dead. With French and Italian politics in turmoil, Europe seems unlikely to be able to make the tough decisions necessary to get a deal done. In that dismal climate, you can hardly blame the White House for moving one of its few stars elsewhere.

Nor is the news all bad on trade—especially, as Mr Hu might note, where China is concerned. Paradoxically, Mr Portman's move suggests that the Bush administration is less worried about congressional protectionism than it used to be. In his year as trade representative Mr Portman, along with his counterparts at the Treasury, worked hard to deflect the more egregious anti-China bills jostling through Congress. He produced a “top to bottom” review of trade policy towards Beijing, designed to mollify irate congressmen without pandering to protectionist instincts.

The strategy seems to be working, at least temporarily. In the build-up to Mr Hu's visit, Sino-American trade tensions have ebbed noticeably. That is partly because the Chinese have made several (small) co-operative gestures. In recent weeks, the Beijing government has promised to end its ban on American beef, to try harder to respect intellectual-property rights, to abide by international rules for government procurement and to allow Chinese firms and citizens to buy more dollars and invest them abroad. The yuan has continued to rise, though marginally.

At the same time, Washington's sabre-rattling has subsided. The Treasury now seems less likely to brand Beijing a currency manipulator when its semi-annual report is released later this month. Senators Charles Schumer and Lindsey Graham have once again postponed their legislation that would impose 27.5% tariffs on Beijing unless the yuan rises sharply.

The front-runner now among Capitol Hill's China-bashing bills is a plan by Senators Charles Grassley and Max Baucus to punish countries with “misaligned currencies” by, for instance, opposing loans from international institutions and blocking any increase in their influence with the International Monetary Fund. Though this would be bad news for IMF reform (see article), it is less disastrous than rampant protectionism.

No one expects the Beijing-bashing to ease up for long, especially with the mid-term elections looming. But, for now, fending off Capitol Hill's protectionists is less important than shoring up support for the administration's domestic priorities, particularly its floundering budget.

Mr Bush's domestic agenda is in tatters. Reform of Social Security, the state pension system, is dead. Tax reform, although presented as a priority, was never attempted. More recent initiatives, such as rejigging the tax incentives on health care, fell off the radar screen almost as soon as they were announced. This year's budget wrangles promise to be a nightmare. The House has not been able to agree even on the outlines of a budget. The Senate's version is dramatically different from the president's. There is little appetite among lawmakers for taking on the (modest) cuts that Mr Bush has proposed in Medicare, the huge federal health plan for the elderly.

Can a new team at the White House sort out this domestic mess? Some signs are encouraging. Mr Portman is not just a heavy hitter on Capitol Hill, he is a budget expert. To be sure, he follows the party line, believing that fiscal prudence means spending cuts, especially on entitlements, and that higher taxes of any sort must be avoided. But as an avowed advocate of transparency and budget rules, he may at least minimise the obfuscation and dubious accounting that have characterised recent budgets.

Although Mr Portman is a clear asset, much depends, too, on who replaces John Snow at the

Treasury. The president is known to be keen to lose him, but cannot find anyone serious to take his place. If the treasury secretary were treated as a policymaker rather than a salesman (admittedly a long shot), Mr Bush might have the makings of a respectable economic team. Better late than never.

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Scott McClellan's departure

A voice of muddle, muzzled

Apr 20th 2006 | WASHINGTON, DC
From The Economist print edition

Making a few improvements with November in mind

AFP

Heading for that rocking chair

ON APRIL 18th, President George Bush's press secretary explained the week's first reshuffle to reporters. “Well, when you have a new chief of staff coming on, the chief of staff, as I talked about yesterday, in the senior staff meeting talked about this is a time to refresh ourselves and re-energise the team,” said Scott McClellan. By his standards, that was quite articulate. The next day, he was gone.

A profile in this month's *Vanity Fair* described Mr McClellan as “the living symbol of this White House's profound and, perhaps, mortal problem with language and meaning.” His resignation was greeted with relief on the right and crowing on the left. “Not to hit a guy when he's down, but...thank God,” wrote John Podhoretz in *The Corner*, a blog attached to the conservative *National Review*. Donna Daugherty, a left-wing songstress, wrote a ditty to mark the occasion, with the chorus: “My name is Scotty, and oh, how I lie!”

The president was kinder, of course. He praised Mr McClellan's “class” and “integrity”, and added: “One of these days, he and I are going to be rocking on chairs in Texas, talking about the good old days.” Sympathetic analysts downplayed the news. Karlyn Bowman of the American Enterprise Institute, a conservative think-tank, thought the story would have “no impact on public opinion” because few Americans could name Mr Bush's spokesman.

That is true, but a president's spokesman has a role in shaping political debate that does not depend on people knowing his name. His justifications of Mr Bush's policies are posted on the White House website and endlessly dissected online. If he cannot explain complex issues clearly, or parry reporters' thrusts, he does his boss a disservice.

No replacement had been named as *The Economist* went to press. But many observers think that, regardless of who the new spokesman is, Mr Bush's chief megaphone will be Karl Rove, his long-time adviser. Mr Bush this week gave one of Mr Rove's titles, that of deputy chief of staff in charge of policy, to a new man, Joel Kaplan. This was reportedly to allow Mr Rove to concentrate on helping the Republicans do less badly than predicted in November's elections. “They're certainly going to need him,” says Ms Bowman.

New Orleans

Flooding back?

Apr 20th 2006 | NEW ORLEANS
From The Economist print edition

A new plan to help New Orleans could go dangerously wrong

AT THE Rock 'n' Bowl one recent evening, as the ancient but brilliant Snooks Eaglin played blues guitar and the smell of gumbo and crawfish filled the air, it was easy to believe that New Orleans was back. The legendary nightspot, famous for offering bowling and Zydeco bands under the same roof, was packed to the rafters. Its motto, “Rock 'n' Bowl will never die!” seemed that of the city too.

AP

Rebuild and damn the consequences

But don't be fooled. New Orleans is far from thriving. The short drive from the French Quarter out to the bowling alley reveals block after block of devastation. Even the strip mall in which Rock 'n' Bowl sits is now empty. Many locals have held back from rebuilding, waiting for word of the official redevelopment plan.

Rumours swirling in March suggested that the levees would not be rebuilt to protect the whole city, and that people would be prevented from rebuilding their low-lying homes. Now salvation appears to have come from the unlikeliest source—the Bush administration, which bungled the aftermath of Hurricane Katrina. On April 12th, the Federal Emergency Management Agency (FEMA) issued long-awaited guidelines on how houses in the area must be rebuilt if they are to qualify for money from state and federal programmes.

Those guidelines, as it turns out, are remarkably unstringent. They could allow most residents to return to most parts of the city and receive government money with only modest upgrades (raising houses only three feet in many cases, not ten or more as anticipated). The federal government also promises that most of the region's flood walls will be replaced and its levees strengthened. The first phase of repairs is to finish by June, and the whole job by 2010.

The plan has gone down extremely well with locals, but their celebrations may be premature. For one thing, these new, non-binding guidelines are not FEMA's final “flood maps”, which are not

expected until later this year. Also, the Interagency Performance Evaluation Taskforce (IPET), a panel of experts commended by the army's own corps of engineers, will not be producing its final report on what went wrong with the city's defences until June—and may yet scotch all plans to rebuild the city's lower-lying wards. If the boffins suggest that those wards cannot be defended economically, it would once again be mostly poor and black residents who would be affected.

Why would federal officials announce such lenient rules before the scientific work is finished? Some see election-year politics at work. By issuing “preliminary” guidelines that prove to be wildly popular, goes this argument, the Bush administration can at last appear to be helping New Orleans back on its feet—and if the IPET report is damning, it can simply blame the boffins.

One federal official offers a more honourable interpretation: “We wanted to kick-start the redevelopment here.” That sounds helpful, but it may be folly to rebuild large parts of the city. The levees, even if built properly this time, will not offer adequate protection for all districts against the flooding that is likely to accompany the most powerful hurricanes. John McIlwain of the Urban Land Institute, a think-tank, argues that it would be much safer and cheaper to rebuild a smaller, denser city for all returning residents in the higher neighbourhoods.

In the end, argues Oliver Houck of Tulane Law School, the new guidelines are “a compromise based on politics, not science. When the flood comes, New Orleans will regret it—but until then, it is great for the economy.” That was ever the city's attitude to life, and death.

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California

The charm of rehab

Apr 20th 2006 | LOS ANGELES
From The Economist print edition

A humane and sensible policy slashes the prison population

"PROP 36 saved my life," says Scott, a much-tattooed 48-year-old who believes he has finally conquered 33 years of drug addiction. "No doubt about it." No doubt, too, that Proposition 36, passed by 61% of California's voters in November 2000 and in effect since July 2001, is saving the state a great deal of money by offering treatment instead of incarceration for non-violent adult drug offenders.

A state-commissioned study released last week by the University of California at Los Angeles calculates that for every dollar invested in Proposition 36 programmes, California has saved $2.50—a total of $140.5m in the first year alone, and $158.8m in the second. Happily extrapolating from UCLA's figures, the Drug Policy Alliance reckons savings over the first five years will add up to $866.5m—plus another $500m saved by not having had to build yet another prison.

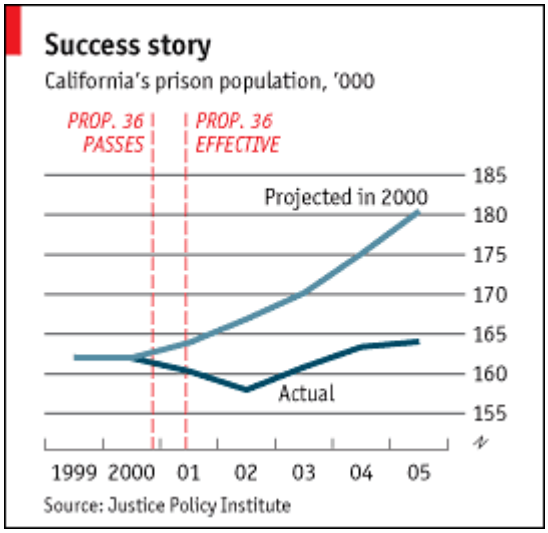
Yet Proposition 36's advocates are feeling uneasy. Money for the programme, $120m a year for five years, runs out at the end of June, and Governor Arnold Schwarzenegger is proposing that it continue only if the legislature passes a bill to reform it, notably by allowing judges to impose brief jail terms for offenders who miss appointments or commit other lapses in their treatment. According to Dave Fratello, a co-author of the proposition, such "flash incarceration" puts the whole principle of Proposition 36 at risk. The riposte from Denise Ducheny, the state senator sponsoring the bill, is simple: "We need to increase accountability."

They both have a point. The basis of Proposition 36, properly known as the Substance Abuse and Crime Prevention Act, is that drug addiction is a disease, and so relapses are to be expected. The trouble is that three out of every ten drug-users referred for treatment never show up; only a quarter of all those referred actually complete their course of treatment; and a disproportionately large share of the cost to taxpayers is being soaked up by a mere 1.6% of Proposition 36 offenders, with five or more convictions in the 30 months before they entered the programme. Such an offender, say the UCLA researchers, costs more than $21,000, compared with less than $2,300 for the "typical offender". By contrast, someone who completes a course of treatment (90 days or more) will save the taxpayer $4 for every dollar spent.

Most Californians appear happy with the programme. In May 2004 some 73% told a Field poll that they would vote again in its favour. But would they be happy to increase its funding? More than 36,000 offenders enter the programme each year, and the number is increasing. In real terms the proposed continuation at $120m a year is a cut in funding, not just because of inflation but also because California's counties had been using money left over from previous years; Los Angeles County alone will lose $16.9m, a cut of 56%. The counties think spending should be increased.

On the basis of the UCLA study, and a simultaneous one
by the Washington, DC-based Justice Policy Institute

(JPI), that would make sense. The JPI notes that before Proposition 36 was passed, California's Department of Corrections was predicting a prison population of more than 180,000 by June 2005 (see chart); the reality, thanks mainly to a 20% fall in imprisonment for drug offences, was a still-horrendous 164,000. At the same time, California's violent-crime rate declined, and faster than the national average. Why not, muses the JPI, extend eligibility for Proposition 36 from simple drug possession to “drug-involved” property offences?



That, however, may be asking too much in a state where the prison guards are big contributors to any politician's coffers. The achievements of Proposition 36 are real enough, but so too is the drive to get re-elected. Cynics note that while the governor talks of the need for rehabilitation rather than punishment in reforming California's colossal corrections system, his push for $68 billion in taxpayers' bonds is designed, in part, to build two new prisons and provide 83,000 new jail beds.

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New York

The white gloves are off

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From The Economist print edition

Rich city-dwellers face the chore of opening their own doors

DOORMEN are as quintessentially New York as the Statue of Liberty, yellow cabs and bagels. So ingrained are they in the culture that Jerry Seinfeld devoted an entire episode of his television comedy series to a doorman, and in “Sex and the City” the sassy redhead, Miranda, was dumped by her boyfriend via the doorman. (“I'm sorry, Ms Hobbes, Jonathan won't be coming down. Ever.”). But thousands of New Yorkers may have to schlep their own rubbish to the kerb and kiss off their own girlfriends if the city's powerful doormen's union goes on strike.

The union, Service Employees International's Local 32BJ, represents 28,000 doormen, porters, lift operators, handymen and other residential-building staff. The union is preparing for a walk-out when its contract expires on April 21st. The two sides are still very far apart: negotiations have been going on all week. The most contentious issues, as in most American labour disputes, are wages and, especially, the provision of health care.

The Realty Advisory Board on Labour Relations, which represents owners and management, has proposed a one-year salary freeze. It also wants union members to take on 15% of health-care costs. Management currently pays the health premiums for all union members, but the board argues that the rising cost of health care is creating huge financial pressure, as are the skyrocketing operating costs.

Union leaders say that they just want an annual cost-of-living increase. But members are also worried about their pensions and health benefits and do not believe the board's cries of poverty. It is no secret that property in New York commands the highest price in the country per square foot in rentals and sales. And having a doorman can add up to 15% to the value of an apartment. Even to apply to live in some luxurious apartment buildings, applicants must be worth millions of dollars.

The question of who contributes what to health-care provision was one of the chief sticking points that prompted New York's transport workers to strike in December. New municipal contracts for teachers and the police included moderate wage increases coupled with “give-backs” (for instance, longer work days or increases in productivity). The doormen's union is determined to avoid any such concessions.

Unlike the other claimants in recent labour disputes, the doormen have the support of New Yorkers—at least for now. Most tenants are so close to their doormen that they think of them as family. The dynamic between tenant and doorman was examined in a recent book by Peter Bearman, a sociology professor at Columbia University. Mr Bearman noted that in the previous doormen's strike, which lasted 12 days in 1991, the doormen helped tenants prepare for their absence, after which most residents were glad to pitch in by mopping floors or screening visitors. Some even provided coffee and doughnuts for their beloved doormen picketing at their door.

This may well happen again. Already doormen are showing tenants how to work the lifts and the security cameras. Some buildings are hiring security guards to take over if the strike goes ahead. Deliveries will be a problem. UPS, a parcel service, has said that its drivers won't cross any picket lines; Fresh Direct, an online food delivery service, is encouraging its customers to place orders now. No one will be allowed to move in or out of an apartment. Perhaps worst of all to the fastidious and those with appearances to keep up, rubbish chutes will be closed.

But there it is. Some 3,500 residential buildings could be hit if there is a strike, and up to 1m New Yorkers may have to hail their own cabs, walk their own dogs and pick up their own dry-cleaning.

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The New York Times

A punch for Pinch

Apr 20th 2006
From The Economist print edition

A bank dares to challenge the Sulzberger family's control of the New York Times

NEWSPAPERS are faring badly in America. Their circulations are falling as the young get their news from the internet, and they are losing their share of advertising, especially classified ads. Last year shareholders in the second-biggest, Knight Ridder, forced the firm to sell itself. No-one made much fuss apart from its journalists. But now the most illustrious publisher of all is under fire. This week Morgan Stanley, an investment bank, launched an unusual attack on the New York Times Company.

Morgan Stanley's investment-management division, which owns 5.6% of the New York Times Company, points to the disastrous performance of the firm's shares, which have fallen by 30% in the twelve months to March. Operating profits have fallen in each of the past three years. Because of a dual share structure in which the controlling Sulzberger family owns special “B” shares with the right to elect nine out of 13 board directors, Morgan Stanley complains, other investors are powerless to intervene. The bank is demanding that the Sulzbergers' special class of shares be abolished, and as a protest it refused to vote for board directors at the firm's annual meeting on Tuesday. Other investors are unhappy with the company too; 28% of ordinary shares were withheld in total.

Tough times for newspaper companies are showing up weaknesses in their managements. In January, Dow Jones & Company, publisher of the *Wall Street Journal*, replaced its chief executive. Some people reckon that Arthur Sulzberger, chairman of the New York Times Company, and his chief executive, Janet Robinson, are simply not doing a good enough job of steering the firm through a changing market. “They've not been as forward-thinking strategically as you would expect from such a powerful franchise,” says Lauren Rich Fine, a publishing analyst at Merrill Lynch.

Morgan Stanley is unlikely to get its way, since the Sulzberger family is unlikely to cede control. But Mr Sulzberger has already presided over two inglorious episodes at the paper—the Jayson Blair affair in 2003, when a reporter was found to have made up parts of his articles, and the recent departure of Judith Miller after flawed reporting on Iraq. Though its purpose may be chiefly symbolic, Morgan Stanley's campaign is a further blow.

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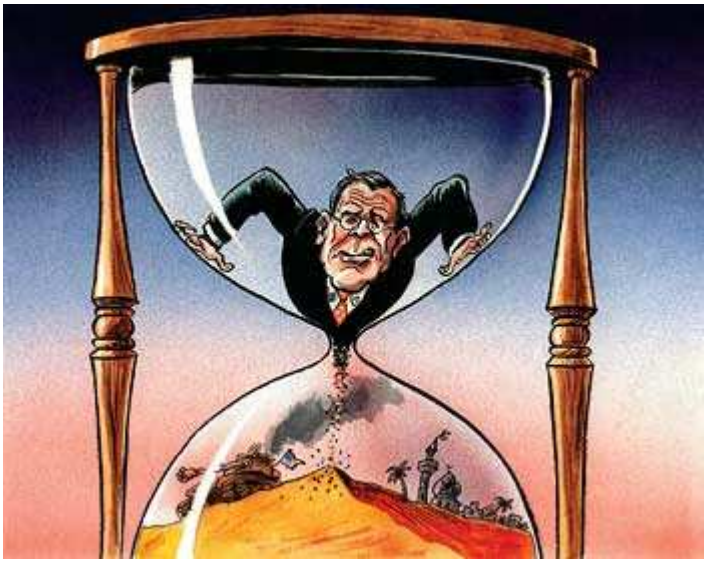
Lexington

Time for him to go

Apr 20th 2006
From The Economist print edition

George Bush is a fool for keeping Donald Rumsfeld in his job



IN THE innocent days before September 11th 2001, a popular parlour game in Washington was guessing when Donald Rumsfeld would be given the boot. The new secretary of defence had managed to alienate both Congress and the Pentagon bureaucracy. And the press was full of stories about his abrasive style and pig-headed arrogance.

September 11th transformed a has-been into a national hero. Mr Rumsfeld immediately captivated the country by running into the burning Pentagon to rescue the wounded. And he kept it captivated with a series of press conferences that projected a mixture of defiance and determination. This was American manliness at its best. The staid *Wall Street Journal* called him a "hunk". George Bush took to referring to him as "Rumstud".

Then came the Iraq war and the disgrace of Abu Ghraib; and this paper, among many critics, called for Mr Rumsfeld to go (see article). Now he is under fire once again. As before, Mr Bush has pledged support for him: "I am the decider and I decide what's best." And Mr Rumsfeld is fighting hard for his political life. He has dismissed the calls for his resignation as a passing storm and a silly fad. Why dismiss the defence secretary, he asks, just because "two or three" people disagree with him?

But the current furore can't be brushed aside. Six retired generals have publicly called for the secretary's resignation. This is extraordinary in itself. But it comes on top of a mountain of other problems. Senior politicians such as Joe Biden and John McCain have been calling for his head for

months. And a series of books—most notably “Cobra II” by Michael Gordon and Bernard Trainor (Pantheon)—have provided yet more ammunition for Mr Rumsfeld's critics. The secretary of defence has become a liability that Mr Bush's troubled administration can no longer afford: a distraction at home and a barrier to success in Iraq.

There is now widespread agreement on what he got wrong. His biggest mistake—the *fons et origo* of all the others—was to try to fight the war with too few troops. His second-biggest was to make no proper provision for restoring order afterwards. But there is no shortage of other mistakes. Mr Rumsfeld misread the intelligence in the build-up to the war, and much of it was simply wrong in any case. He failed to plan for the occupation. He ignored the growing insurgency. He disbanded the Iraqi army, scattering 300,000 armed and unemployed men into the population. The more interesting question is why he messed up so comprehensively.

The most obvious reason, of course, is arrogance. Mr Rumsfeld suffered from exactly the same problem as another whizz-kid CEO turned secretary of defence, Robert McNamara: iron self-confidence. He junked the army's carefully laid plans for invasion (General Zinni's plan called for at least 380,000 troops, for example, far more than Mr Rumsfeld sent). He dismissed warnings from General Shinseki that it would take hundreds of thousands of troops to win the peace. He ignored pleas for more troops on the ground. And he surrounded himself with similarly one-dimensional strategists such as General Franks and yes-men like General Myers.

Another reason is bureaucratic turf wars. Henry Kissinger once described Mr Rumsfeld as the best practitioner of the art of bureaucratic infighting that he had ever seen, which is no mean compliment; and he certainly did a brilliant job of elbowing Colin Powell and the State Department aside, putting control of post-war reconstruction in military hands for the first time since the second world war. But he had no idea what to do with his new-found power. Without the State Department's experience of post-war reconstruction, gathered in Bosnia and Afghanistan, Mr Rumsfeld veered all over the place.

Virtue's flip side

The biggest reason that Mr Rumsfeld made such a mess of things was that he was fighting the wrong war. His greatest passion was to “transform” the lumbering old army into a much lighter and more flexible force, and he seized on Iraq as a perfect opportunity to demonstrate it. In a few short weeks, American troops victoriously took Baghdad—but then failed completely to impose control and end the violence. The defence secretary's insistence on “lean warfare” made it impossible to seal the borders or stop the looting; his reliance on high-tech weaponry rather than boots on the ground made it difficult to crush the insurgency; and, according to the non-partisan Schlesinger commission, his insistence on junking long-established planning procedures contributed directly to the disgrace of the prisoner-baiting at Abu Ghraib, because the chain of command was disrupted and commanders found themselves in charge of units that they didn't know.

The tragedy of Mr Rumsfeld is that his vices are the flip side of his virtues. He was right that the American armed forces had barely woken up to the end of the cold war. He was right that the Pentagon bureaucracy is one of the most reactionary in the world. And he was right that, with very precise air-strikes based on good intelligence, minimum muscle could be used in modern warfare. But Mr Rumsfeld ended up suffering from the very problem that he saw in his critics: a failure to adjust his thinking to new circumstances. He allowed “transformation” to distract attention from the war (army officers accuse him of “trying to fix the car while the engine's running”). And he mistook criticism as a sign of bureaucratic resistance.

But this is a tragedy that America can no longer tolerate. Getting rid of Mr Rumsfeld is no

guarantee that things will get better. But keeping him ensures that they will get worse. Mr Bush made a huge mistake in not accepting Mr Rumsfeld's offer to resign in the wake of Abu Ghraib. Every day he keeps him in his job he compounds his mistake and weakens his presidency.

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Mexico's presidential election

The front-runner under pressure

Apr 20th 2006 | IGUALA
From The Economist print edition

With his opinion-poll lead wobbling, Andrés Manuel López Obrador has yet to define precisely what sort of change he stands for

AFP

THE crowd in this small town in Guerrero, one of Mexico's poorest states, is full of middle-aged men wearing traditional sombreros. It is parted down the middle by a pair of cordons, which clear a path for Andrés Manuel López Obrador, the presidential candidate of the centre-left Party of the Democratic Revolution (PRD). He turns to the left, and to the right. He is where he wishes to be seen to be—in the centre. He shakes hands and slaps backs with the smile of a practised campaigner, but not a natural one. The stump speech is competent, but it is the content rather than any oratorical flourish which draws cheers. He will cut the president's salary in half and those of other senior officials as well, he says. The elderly, children and the disabled will get monthly grants. With each pledge, the crowd cheers: “Ob-ra-dor!”.

With such promises, Mr López Obrador has topped opinion polls for many months. But with ten weeks to go before the election on July 2nd, his lead seems to be narrowing. Two of the latest polls put Felipe Calderón, the candidate of the conservative National Action Party (PAN) of Vicente Fox, within four points. In third place in most polls, hindered by scandals, is Roberto Madrazo of the formerly ruling Institutional Revolutionary Party (PRI).

So the long campaign is moving into its decisive phase with Mr López Obrador on the defensive. Reflecting his uncertain position, he has refused to take part in the first of two candidates' debates, on April 25th, but is expected to appear in the second.

For now, at least, the election remains Mr López Obrador's to lose. Yet it is still unclear what sort of president he might be. He is reflexively supported by many poorer Mexicans, who are drawn to his populist rhetoric. That same rhetoric has inspired fear and hatred among richer Mexicans, who disbelieve the candidate's insistence that he would “respect macroeconomic norms” and their property.

His record as mayor of Mexico City in 2000-05 gets similarly mixed reviews. Several corruption scandals rocked the city government on his watch—but had little impact on his public image. That was largely because, like Mr Calderón, he is seen as personally honest. He drives a cheap car and lives in a middle-class apartment. “His austerity is sincere,” says Sergio Aguayo, a Mexican political analyst.

But he did not transform the capital, as his campaign rhetoric suggests. Crime continued in Mexico City, and if he did not know of the corruption in the city government, he should have, says Soledad Loaeza, a political scientist at the Colegio de México, a graduate school.

The central point of Mr López Obrador's campaign is that Mexico's political system needs changing. He presents this not as an ideological issue, but as a commonsense clear-out of corruption and privilege. In this, his campaign is not dissimilar to that of Mr Fox, who ousted the PRI in 2000 after seven decades in power with the slogan of “Change!” but then failed to deliver much of it.

Mr Aguayo says that rather than Mr Fox changing Mexican politics, Mexican politics changed him: “Fox became one of them. Psychologically he wanted to beat the PRI, not destroy the system.” Mr López Obrador, on the other hand, seems to want fundamentally to alter things. But how? He has reached beyond his party to set up “Citizen's Networks”. These could help turn the PRD, founded by populist renegades from the PRI and small leftist groups, into a modern social-democratic party—or they could become agents of a personality cult revolving around Mr López Obrador, says Mr Aguayo.

The candidate has assembled a respected team of advisers. But some doubt he would listen to them. According to Luis Rubio of CIDAC, a Mexico City think-tank, the problem, in a phrase coined by Winston Churchill, “is not that he is ignorant, it is that he knows too many things that are not true.” For example, cutting wages of top officials will not pay for social programmes (but might encourage corruption and mediocrity). Mr López Obrador's solution to Mexico's energy problems is to allow Pemex, the inefficient state monopoly, to spend more, rather than invite private investment. For all his talk of reform, he will avoid open government if he can, says Mr Aguayo.

Mr López Obrador's defining quality—or flaw—is a belief that he knows best and is uniquely capable of changing a system of which he is very much a product. He spent his formative political years as a PRI operative and was loyal to two of its most populist presidents. Many Mexicans believe that a López Obrador victory might presage a PRI restoration in disguise.

Others fear that it might propel Mexico along the path of Hugo Chávez's Venezuela. Mr Calderón has risen in the polls after an advertising blitz attacking Mr López Obrador as an agent of *chavista* chaos. The former mayor looks more of a pragmatist than an ideologue. In that, he resembles Brazil's president, Luiz Inácio Lula da Silva. Some of his goals—to tackle monopolies and the cosy links between business and politics, for example—are good ones.

But his speeches are often aggressive and divisive. He seems to have done himself no favours by repeatedly comparing Mr Fox, whom Mexicans still respect, with a *chachalaca*, a particularly noisy turkey-like bird. His populist demagoguery, his political origins and his patchy record as mayor are all reasons to mistrust Mr López Obrador. It is clear that Mexicans want change. As he comes under pressure in the campaign's final stretch, it may become clearer whether he represents a change for the better or for the worse.

Venezuela

Crimes and misdemeanours

Apr 20th 2006 | CARACAS
From The Economist print edition

Discontent hits the streets

THREE teenage brothers were kidnapped with the family chauffeur on their way to school in Caracas on February 23rd. Forty days later, the bodies of all four were found outside the city. The discovery produced a wave of outrage, much of it directed against the government of Hugo Chávez, Venezuela's socialist president. Since he took office in 1999, the country's murder rate has almost tripled.

For once, the protests seemed spontaneous, despite the efforts of officials to pin them on their opponents. The opposition denounces—and has tried to topple—Mr Chávez for curbing democracy. But oddly it has failed to take up issues on which the president is most vulnerable, such as corruption, jobs and crime.

AP

Be afraid

Caracas has become South America's most violent capital. Worse, the police are themselves suspects in many of the killings. The public prosecutor's office says it is investigating over 6,000 alleged “extra-judicial executions” by police. The brothers were kidnapped by men in police uniform, as was a businessman kidnapped and murdered last month. Two dozen policemen are currently awaiting trial for killing three students, and wounding three others, who failed to stop at a roadblock.

The vast majority of murders take place in the anonymity of the slums, and never come to public attention. According to some accounts, gang-members have been recruited into the police to enforce political control rather than fight crime.

Mr Chávez will seek another six-year term at an election in December. The government wants to shift the political debate away from bread and butter issues. So Mr Chávez is claiming that what is at stake in the election is an ideological conflict between the United States and Venezuela's “Bolivarian revolution” and that his true opponent will be George Bush. Earlier this month police stood by as a crowd of *chavistas*, some on motorbikes, pelted the American ambassador's car with eggs after he donated baseball equipment to a school in a poor area of Caracas.

Such circuses may not deflect the grievances of ordinary Venezuelans. In the past two months there have been at least 30 demonstrations demanding that the government fulfil its promises in matters such as housing and jobs. Mostly leaderless, the protests mix *chavistas* and non-*chavistas*, although most of the latter do not support the opposition. The government's approval rating was only 14% in a recent survey by Hinterlaces, a polling firm.

Many Venezuelans have hitherto been inclined to absolve Mr Chávez of personal blame. But their discontents provide scope for an independent candidate not identified with the discredited opposition. One who may try to fit the bill is Teodoro Petkoff, a onetime leftist guerrilla leader who was planning minister in the last pre-Chávez government and who is now a newspaper editor. Since Mr Chávez controls all the institutions of state, and is spending a massive oil windfall, he is widely assumed to be unbeatable. But as the demonstrations show, he does not always control everything that happens in his country.

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Colombia

Unintelligent

Apr 20th 2006 | BOGOTÁ
From The Economist print edition

A compromised secret police

THE timing of the revelations—just weeks ahead of a presidential election on May 28th in which Álvaro Uribe is seeking a second term—was surely not coincidental. But that did not diminish their explosive nature. Earlier this month, several Colombian publications reported claims that the former head of the Administrative Security Department (DAS)—the secret police—had worked hand in glove with leaders of Colombia's right-wing paramilitaries to murder trade-union leaders and thwart operations against drug-traffickers.

The allegations came in interviews with Rafael García, a former DAS official. He was arrested last year on charges that he doctored files on paramilitary chiefs and drug-traffickers wanted for extradition to the United States. He wants a plea bargain in exchange for testimony against the former head of the DAS, Jorge Noguera, whom he accuses of close links with paramilitary bosses on Colombia's Caribbean coast. The DAS had given the paramilitaries a list of labour leaders in that area to be targeted for murder, several of whom were later killed, he said.

Most of these claims are not new. They seem unlikely to hurt Mr Uribe electorally. Polls suggest he will win over 50% of the vote. Most Colombians support the president's tough-minded security policy, which has seen violence fall steadily. In a controversial peace agreement, he has secured the demobilisation of the 30,000-strong paramilitaries, the last of whom handed in their arms this month.

But the saga of the DAS revealed two of the president's flaws. The first is his thin skin. His response was to rail against the media for reporting the scandal. The second is that he has not always shown good judgment in his appointments, such as that of Mr Noguera. To compound matters, when the allegations against Mr Noguera first surfaced, Mr Uribe sent him to Milan as consul. (Mr Noguera denies the claims. He has returned to Colombia to answer prosecutors' questions, and threatened to sue the media for defamation.)

There is much evidence that the paramilitaries and drug-traffickers—often the same people—have infiltrated not just the DAS but many other institutions in Colombia. These include the public prosecutor's office, which has named a team of investigators to look into Mr García's claims. This problem predates Mr Uribe. The presence of infiltrators does not mean that Colombia is a “paramilitarised state”, says Alfredo Rangel, a security analyst.

In October, Mr Uribe named Andrés Peñate, his capable former deputy defence minister, to head the DAS with a brief to clean it up. Mr Peñate set up an outside advisory commission, which called for the DAS to refocus on “strategic intelligence”.

But what the agency needs is root-and-branch reform or closure, argues Sergio Jaramillo, a former defence official now at Ideas for Peace, a think-tank. Its original purpose was to exercise

political control. Its bosses are political appointees, and it lacks not just a clear role but a career structure and esprit de corps. While Colombia's police and army have modernised, the DAS has not, he says.

Mr Uribe is “not sensitive to the international perception” that criminal influence over the state is on the rise, according to Myles Frechette, a former American ambassador to Bogotá. Tackling this is a task for his second term—assuming the scandal does not impede his re-election.

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Argentina

Uneasy peace

Apr 20th 2006 | BUENOS AIRES
From The Economist print edition

A return of labour militancy

IT HAS not been necessary to pick up a newspaper this month to recognise the disruptive power wielded by Argentina's labour unions. On the streets of Buenos Aires, this has assailed the ears and nose. Just before Easter, 70 subcontracted security guards and janitors shut down the city's metro system for two days, demanding to join the public-transport workers' union. The strike added some 250,000 honking cars to rush-hour traffic. A week earlier, piles of rubbish swelled across pavements in Buenos Aires province after the truck-drivers' union stopped collecting it in pursuit of a 28% salary rise.

The wave of strikes is both a cause and a consequence of resurgent inflation. In the aftermath of Argentina's economic collapse of 2001-02, idle factories and mass unemployment kept prices stable and unions quiet. But last year—the third of 9% annual growth—inflation rose to 12.3% as shortages of skilled labour and capacity surfaced in some sectors. Emboldened by their increased leverage and angered by the fall in their members' purchasing power, the unions emerged from hibernation. In the vanguard were the transport workers, whose 112 separate strikes in 2005 was the highest figure for 18 years.

Argentina's president, Néstor Kirchner, has opted to keep growth going rather than raise real interest rates or allow the currency to appreciate to damp down inflation. Instead, he has sought “voluntary” price freezes from retailers. He hopes these will keep inflationary expectations in check while he tightens fiscal policy.

But the unions could throw a spanner into this strategy. Big wage increases would destroy the president's prized price accords, since they remain valid only as long as business costs do not increase. Granting a big increase to public employees, whose wages lag behind the private sector and who begin negotiations this week, would knock a hole in the budget.

To avoid raising inflation, wage settlements must be kept below 20%, the government and independent economists agree. But Mr Kirchner, who hails from the left wing of his labour-based Peronist party, finds it hard to say no to union leaders. He stepped in to end the rubbish strike, offering a 19% wage increase at a meeting with Hugo Moyano, the truculent truckers' leader who also heads Argentina's largest labour confederation. He had earlier offered Mr Moyano other juicy incentives. His union was granted a share in a rail line and a big increase in government payments to its health-care scheme. One of its lawyers was named to head a federal credit agency with a $110m budget.

The problem for the president is that Mr Moyano has only a partial grip on the labour movement. His faction won control of the General Labour Confederation, which negotiates for a third of the workforce, by ousting another group known as *los gordos* (“the fat cats”) because of their profitable business deals during the 1990s. The fat cats may seek revenge by pushing for strikes

to bust the 20% barrier. For now, Mr Kirchner and the unions are at peace, but it is an uneasy one.

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Quebec separatism

Coming out as Canadians

Apr 20th 2006 | MONTREAL
From The Economist print edition

A heresy that dare not speak its name

ARTISTS of various kinds have long been among the most ardent supporters of an independent Quebec. So it came as a surprise when the province's two best-known playwrights admitted to having lost some of their faith in separatist politics. But so intolerant has been the reaction that their convictions may have been further undermined.

Michel Tremblay has been a pillar of the province's cultural establishment since the 1960s. In a casual interview after a literary event, Mr Tremblay berated separatist leaders for putting economic issues above cultural ones. “As long as the economy is put ahead of everything else, sovereignty will never happen,” he argued. The next day, Robert Lepage, a dramatist and filmmaker, admitted to similar misgivings. “I still have a sliver of sovereignist sentiment within me but I clearly need to be re-convinced,” he said.

Since Mr Lepage's international successes almost rival those of Quebec's most famous exports, Cirque du Soleil and Céline Dion, his comments wounded the *purs et durs* among the separatists.

The two were guilty of “treason” and were suffering from “premature senility”, roared Victor-Lévy Beaulieu, a writer and publisher. Other artists called on them to keep their political opinions to themselves. Politicians joined in. Bernard Landry, a former Quebec premier, hinted that he would boycott Mr Tremblay's plays. The leader of the Bloc Québécois, Gilles Duceppe, phoned the playwright for an explanation.

Mr Tremblay duly assured Mr Duceppe—and later the province—that he still thinks Quebec should be independent. But he asked of the lynch mob: “What are they going to do? Burn my books in the public square because I dare to say something different?”

The brouhaha reflects a genuine quandary for the separatist movement. Its leaders have downplayed culture to broaden their appeal to include immigrant groups and not just native French-speakers. But the spat also underlined that, despite receiving pots of federal money, it is much easier for Quebec's artists to come out as gay (as both playwrights did years ago) than to reveal the merest suspicion of closet federalism.

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South Korea and its conglomerates

The wages of atonement

Apr 20th 2006 | SEOUL
From The Economist print edition

Camera Press

Saying sorry is a delicate business—and an expensive one

IN NO capitalist country is economic power so concentrated as in South Korea—and you would probably have to look to North Korea for a greater concentration in Communist ones. Industrial production, in particular, is dominated by a handful of family-controlled conglomerates, called *chaebol*. The Samsung group, the biggest of the lot, alone employs more than 130,000 workers. It accounts for a fifth of South Korean exports and a significant chunk of government revenues. The second-biggest, the Hyundai-Kia group, makes nearly three out of four of the vehicles on Korean roads and, with new factories planned in America, the Czech Republic and China, is now the world's seventh-biggest carmaker. And Hyundai cars these days are pretty good—certainly not the tinny contraptions of yesteryear.

Until the Asian financial crisis of 1997-98 and South Korea's IMF bail-out, the family-run *chaebol* were useful tools of government policy. In return for providing lots of jobs and driving economic growth through exports, they received cheap financial backing and the freedom to expand into practically any business that took their fancy. After the crisis, however, plenty of observers predicted their demise: their version of crony capitalism was blamed for all South Korea's woes.

Many groups were indeed forcibly broken up by the government, or allowed to fail under their weight of debt. But some *chaebol*-linked firms, notably Samsung Electronics (the most successful bit of the Samsung empire) and Hyundai Motor, emerged fitter and better able to compete on a global scale. Samsung Electronics, for instance, leads the world in memory chips and, among Asian manufacturers, is second only to Toyota in stockmarket capitalisation, having recently overtaken Japan's best-known electronics brand, Sony—for which, incidentally, it makes all its

large flat-panel televisions. And the dominance of the *chaebol* does not persist only in the economic field. The comings and goings of *chaebol*-family offspring play the role of minor royalty in the soap opera of national life. Samsung sponsors not only almost every sports team in the country but also the sporting leagues.

Now, however, the global ambitions of both the Samsung and Hyundai groups are, by their own admissions, in jeopardy as a result of miscalculations by the groups' respective founding families. Their mistake was a failure to notice in time that public expectations about business ethics have been rising—and how readily the authorities are now willing to punish improprieties that used to be overlooked.

Last autumn, the Samsung patriarch, Lee Kun-hee, left South Korea for America, ostensibly for medical attention but seemingly also to escape indictment over alleged illegal political donations during the 1997 presidential campaign. He returned in February, after the statute of limitations had expired, but prosecutors are still looking into the controversial transfer to his children of control of the family holding company through the issue of tax-dodging convertible bonds.

Then, in late March, prosecutors raided Hyundai's offices. In an investigation that is likely to come to a head over the next few days, they have been looking at allegations of slush funds to bribe government officials. They have also been looking at a deal similar to the Lee family's, whereby corporate control of the Hyundai group was quietly passed from the father, Chung Mong-koo, to his 35-year-old son.

These alleged misdemeanours have created public uproar and a national debate that the founding families have found impossible to ignore. When Mr Lee returned to Seoul from the United States, he asked his countrymen, at the airport, for forgiveness. A couple of days later, Samsung said that the Lee family was giving 800 billion won ($830m) “to society”. Not to be outdone, on April 19th, when Hyundai's Mr Chung returned from a ground-breaking ceremony for a new factory in China that he was nearly forced to miss because of the investigation, the company apologised for “causing the public concern and for not taking our full social responsibility as a company that should have been a role model.” Mr Chung and his son, Chung Eui-sun, it was further announced, will also donate to “society” their 60% stake, worth about 1 trillion won, in Glovis, a Hyundai affiliate company that investigators first raided.

Such contrition fees seem to be becoming the rage. Even foreigners are getting in on the act. Recently, Lone Star, an American buy-out fund under investigation for embezzlement and tax evasion by one of its employees, faxed the finance ministry an offer to pay 100 billion won to “society”. Though President Roh Moo-hyun appears to welcome such contributions, at least from the *chaebol*, other South Koreans harbour reservations. One senior official calls Lone Star's offer “skin-deep”, part of a “shameful tradition” that “reinforces the notion that government can be bought off every time something goes wrong.” Jang Hasung, dean of the Korea University Business School, calls such payments an “insult to the public”.

All this may mean that the *chaebol*'s founding families are in danger of misjudging the public mood for a second time. Just as they learnt too late of the public's growing intolerance—as well as scrutiny—of the former sleazy links between business and government, so now they risk underestimating the price of contrition. On the other hand, Mr Jang is possibly right when he calls these latest scandals a “turning-point”. As such big fish in a small pond, one family member says, the *chaebol* need the public's trust at home if they are not to be held back abroad. And there is still a lot more trust to be won.

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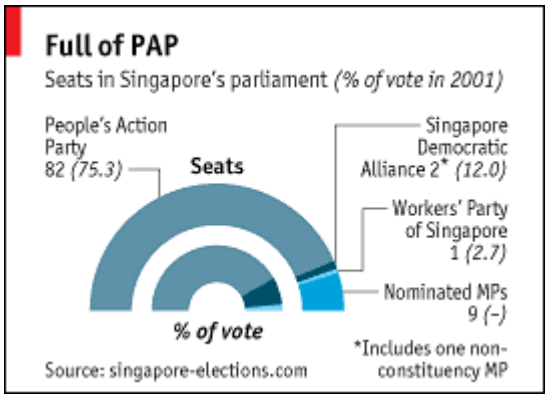
Singapore's election

A rational choice

Apr 20th 2006 | SINGAPORE
From The Economist print edition

Will the affluent young deny the bossy ruling party a clean sweep?


Full of PAP
Seats in Singapore's parliament (% of vote in 2001)
People's Action Party 82 (75.3)
Seats
Singapore Democratic Alliance 2* (12.0)
Workers' Party of Singapore 1 (2.7)
Nominated MPs 9 (-)
% of vote
Source: singapore-elections.com
*Includes one non-constituency MP

SINGAPOREAN television showed an atypically interesting programme last week. In "Why My Vote Matters—A Dialogue with the Minister Mentor", the city-state's octogenarian former prime minister, Lee Kuan Yew, faced a panel of young voters, who made all sorts of criticisms of his People's Action Party (PAP), which has ruled Singapore since independence from Britain in the 1960s. Mr Lee—still a power in the land as cabinet "mentor" to the current prime minister, his son, Lee Hsien Loong—heard his party called "arrogant" and "power crazy" and accused of making people afraid to vote for the opposition.

Many times in the past, the PAP has replied to criticism with lawsuits: earlier this year an opposition leader was bankrupted by libel suits from Mr Lee senior and another former prime minister, Goh Chok Tong, for making allegations about the government's use of public funds. However, on the television show, the minister mentor showed only the mildest signs of irritation at the youngsters' impudence, as he patiently rebutted their accusations and explained "why we do what we do". The show was broadcast, several times, a few days before the government dissolved parliament and announced a new election for May 6th.

The result of the election is not in any sort of doubt. The PAP has continued to fulfil its promise of honest and efficient (if bossy) government. Growth has been strong—9% in the year to March. So another walkover is near-certain. In the 2001 election, the PAP won 75% of the vote. The opposition, which contested only 29 of the 84 constituencies, won only two—though it was awarded a third "non-constituency" seat under the election rules.

Even so, the party seems keen to win a crushing mandate for the younger Mr Lee, who took over in 2004. Perhaps the TV show is a sign that PAP fears that Singapore's affluent youth, unable to recall just how poor and divided Singapore was before Mr Lee senior and his party transformed it, might feel tempted to think of voting elsewhere. At any rate, Mr Goh is masterminding a blitz of the two opposition constituencies, seemingly hoping for a clean sweep. The PAP manifesto includes plans for cheaper health care, answering one of the opposition's main criticisms. And recent budget surpluses are being refunded to the public in a conveniently timed "Progress Package", typically worth around S$800 ($500) for each adult. One of the few issues that might have given the opposition some traction—a financial scandal at the country's National Kidney Foundation—has been dealt with decisively: this week, criminal charges were laid against several of its former bosses.

As Teo Chee Hean, a senior party figure (also the defence minister) puts it, Singaporeans are

rational. The PAP always delivers good government in return for a strong mandate, so he expects it to win one again. Party bosses say too much opposition will only hold the country back. When one of Mr Lee senior's young inquisitioners suggested that a bit more freedom of expression would make the country stronger, he retorted: “You mean to tell me that what is happening in Thailand and the Philippines is binding the people, building the nation?”

Given the PAP's popularity, the opposition has sometimes sought to gain by losing. By contesting only a minority of seats and guaranteeing the PAP victory, it has hoped to encourage people to take the risk of voting for the opposition. This did not get them very far, so this time the various opposition groups will stand in at least half the constituencies. Steve Chia of the Singapore Democratic Alliance, one of the main opposition groupings, says their aim is to win 15 seats and form a shadow cabinet, to provide effective scrutiny for the government. He admits this is ambitious. That's putting it mildly.

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Papua and Australia

Bad neighbours

Apr 20th 2006 | JAKARTA
From The Economist print edition

Why Australia and Indonesia have fallen out over poor Papua

AUSTRALIA'S decision last month to grant temporary political asylum to 42 people from Papua, Indonesia's separatist-wracked half of the island of New Guinea, has caused a collapse in relations between the two big countries. Indonesia's president, Susilo Bambang Yudhoyono, is furious, not least because his promise to Australia's prime minister, John Howard, that nothing untoward would happen to the Papuans, who claimed they would be persecuted if returned, has had no effect.

Mr Yudhoyono has recalled his country's ambassador from Canberra and ordered a review of all official links with his southern neighbour. Insulting newspaper cartoons on both sides have not helped. This week Mr Yudhoyono demanded concrete proof of Australia's support for Indonesian sovereignty over Papua, a territory Jakarta annexed following a rigged referendum in 1969.

Mr Howard has repeatedly insisted the decision was administrative not political and that his government supports Indonesian sovereignty over Papua. In a sop to Mr Yudhoyono, he tightened procedures to deter further asylum seekers last week. But he has refused to apologise, saying the decision was taken in accordance with Australia's laws and the 1951 Refugee Convention, which Indonesia has not signed. The row is steadily getting worse, and will probably need summit-level healing.

Australia is in a bind because Indonesia's policies towards Papua oscillate from concerned support

to brutal repression. Living standards, particularly in urban areas, have risen noticeably in recent years. But decades of resentment over broken promises of greater autonomy and fairer distribution of the cash from Papua's enormous natural resources still simmer. Last month, four people died in protests against an American-owned gold and copper mine there, Freeport McMoRan, regularly Indonesia's largest taxpayer.

At the same time, the Indonesian government still uses wholly disproportionate force to subdue a tiny and poorly equipped Papuan independence movement. All this has left most Papuans at best distrustful of Jakarta and more often wanting to secede from Indonesia. The division of the territory into two provinces in March, despite widespread local opposition, has exacerbated tensions.

In fairness to Indonesia's government, Papuan activists' claims of genocide lack credibility. But Mr Yudhoyono's policy of severely restricting access to the region by diplomats, researchers and journalists means that such allegations cannot be completely discounted. Hopes that Papua will follow Aceh, the Indonesian province blighted by rebellion for 29 years and now on the road to peace, are thus fading fast. And hopes for a restoration of good relations with Australia look little healthier.

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Mapping China, badly

No direction home

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From The Economist print edition

When state secrecy meets modern motoring

FROM May 1st, millions of Chinese will enjoy a week's holiday. But many of those planning to drive long distances or hike in the countryside will get lost. The hectic pace of urban construction and road building combined with a culture of secrecy makes Chinese maps unreliable and vague.

Detailed topographical maps of the kind commonly used by ramblers in other countries are strictly classified. Schoolchildren get no training in how to read them. Two years ago government cartographers in north-eastern China said some local government websites had “seriously threatened national security” by displaying secret maps with contours, elevations and grid lines.

But the internet and the spread of satellite-navigation technology are beginning to weaken the state's control of cartographical detail. Chinese officials were horrified last year when they discovered that users of Google Earth, a free satellite-imaging facility, could direct the software to display buildings inside Zhongnanhai, the Communist Party's high-walled headquarters, together with their precise latitude and longitude. Chinese maps do not even mention the compound.

Chinese companies with an eye on the country's legions of novice, cartographically challenged drivers are racing to develop software for navigation devices using America's global-positioning system (GPS). SinoMaps Press, the only national cartographer in China, has a mere 20 people in its electronic-mapping division. But in recent years things have changed. A handful of independent companies have sprung up employing armies of several hundred people each to drive around cities and gather information for their GPS databases.

These databases must still be examined by the government to ensure they contain no secrets. Your correspondent's navigation software identifies more government buildings than would be found on regular maps, but still not the party headquarters or the ministry of defence. “Even what is secret is a secret,” says Tang Ningzhe, who works for Beijing Lingtu Software, an electronic-mapping company, when asked to describe precisely what it is that his software is not allowed to display.

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India

Defiantly poor

Apr 20th 2006 | COCHIN
From The Economist print edition

But impressively literate

TUCKED away on the south-western tip of India, the small state of Kerala boasts over 91% literacy, low infant mortality and other favourable social indicators. It has also become one of India's most popular destinations for both foreign and Indian tourists. It is ideally sited, where the Arabian Sea meets the Indian Ocean, to be an entrepot for international trade.

For all that, it has little industrial development or foreign investment. Despite a basic education record that outstrips most other states, the per capita income of its 33m population is half that of Goa, India's richest state. It tops India's rankings for suicides and alcohol consumption. It may boast a relaxing natural environment of beaches and tree-lined inland rivers, but this has been no draw to information-technology companies—it provides just 0.4% of India's booming software exports, which are dominated by the nearby states of Karnataka and Andhra Pradesh.

The mismatch stems mainly from an obsession with politics. This is driven by a trade union-led left that has dominated debate and restricted industrial development since the 1950s, and complicated by ageing local politicians reluctant to make way for younger ones. The fascination with politics is noisily evident in campaigning for the state-assembly elections that will start on April 22nd. Posters with the hammer-and-sickle and other parties' emblems are plastered across towns and villages, even appearing on tree trunks and poles along a network of popular “backwaters” that are the state's main tourist attraction. Boats festooned with flags aim loud political broadcasts at small groups listening in the shade of palm trees.

Opinion polls predict that a Communist-led Left Democratic Front (LDF) will win, pushing out a Congress Party-led United Democratic Front (UDF) that has ruled for five years, and continuing a 40-year pattern of no party or coalition winning two consecutive terms. This extreme example of the anti-incumbency factor, as it is known in Indian politics, has bedevilled development, because one government's cherished projects are frequently abandoned by its successor.

The LDF is now querying a software park awarded by the UDF government to Dubai developers, as well as an elevated expressway, the conditions of an Asian Development Bank loan, and private-sector investment that the UDF allowed in engineering and medical colleges. “Black marketeers have come into education,” says M.A. Baby, a candidate for the main Communist party, the CPI (M).

This deters investors, as does the general lack of continuity of government policy, the seemingly endless left-leaning debates, and militant trade unions that close down towns and cities with strikes. Worsening Kerala's reputation, the left wants software workers to be unionised, and work at a Coca-Cola bottling plant has been stopped for two years by local villagers protesting that it depleted and poisoned their water supplies. “We haven't bought into the need for material production,” says Prakash Karat, the CPI(M)'s national leader and a native of Kerala.

For all this, Kerala has been acclaimed by academics, including Amartya Sen, a Nobel-prize-winning economist, as “the most socially advanced state in India”, despite the suicides and liquor intake that stem from frustrated ambitions. Its literacy rate is without equal in the developing world and its life expectancy is over 70 years. The record of strong basic education goes back nearly a century to benevolent local rajas, in what were the states of Travancore and Cochin, and to Christian missionaries—Christians make up 20% of the population. But further education was stymied from the 1960s when the Left insisted it should be in the public sector, which could not afford to expand. Since then, many of Kerala's bright youth have gone elsewhere to study, especially for engineering and nursing, and rarely return, increasing the export of local brainpower. About 20% of the software engineers and call-centre workers in Bangalore are estimated to come from Kerala and, in earlier years, offices across India were staffed by Keralan typists.

The local economy is propped up by $5.5 billion annual remittances from 3.5m Keralans who work abroad, 85% of them in the Middle East. This fuels consumption and a property boom, contributing to an 8% economic-growth rate in the past year. But the money rarely goes into long-term investment—though overseas Keralans funded 36% of a new, highly profitable, $63m airport at the city of Cochin in 1999.

That rare example of enterprise is repeated in the field of tourism, which has boomed in the past six years, driven initially by local businesspeople starting small and largely up-market resorts on the unspoilt backwaters and beaches, and then supported by the government. This has made Kerala India's only significant new tourist destination to be developed for decades. Last year it drew 6.5m tourists, 350,000 of them from abroad compared with 50,000 ten years ago. “That's the left's main contribution—to have kept Kerala green for tourism,” says Jose Dominic, a leading hotelier.

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Nepal

The endgame

Apr 20th 2006 | KATHMANDU
From The Economist print edition

A messy abdication is another compromise?

ASKED whether King Gyanendra consults astrologers the government spokesman gave an answer with which many would sympathise. “I do too,” he said. “If you were in Nepal for quite a while, so would you.”

AFP

All the king's men

After more than two weeks of anti-government protests, few conventional observers feel qualified to peer far into Nepal's future. Ten demonstrators have been killed at rallies across the country. As *The Economist* went to press, Kathmandu was under an 18-hour “shoot-to-kill” curfew, with at least three protesters shot dead on April 20th. The city is short of fuel and fresh food thanks to an opposition-led strike. Crucially, the civil service has joined the protests. Twenty-five officials were arrested at the interior ministry this week, and staff at the national bank are on strike. The entire banking sector is now closed, and cash in short supply.

Many people would also like to know where the king gets his political advice. As the crisis has mounted he has been slow to respond. Initially he stayed at a provincial palace because, rumour has it, a partial eclipse made it inauspicious to return to the capital. Yet it appears the gravity of the situation is slowly dawning on him, though he refuses to refer to the protests. This week he released five leading opposition politicians from government custody. Further attempts at reconciliation may follow, but finding a deal will not be easy. Gyanendra's exaggerated sense of royal dignity is only one obstacle.

Even the opposition parties have been surprised by the depth of republican sentiment revealed during the protests. More than one opposition leader has privately explained that he will be lynched if the parties fudge a deal with the palace as they have in the past. That creates a

problem for the leaders, who demand a new constitution but not necessarily a republic. Party planners fear that rapid progress to a republic could allow their loose allies, the powerful Maoist rebels, to fill the vacuum.

Opinion is divided over the likelihood of the government falling. The American ambassador infuriated the Nepali government this week when he predicted a messy abdication with the king clinging to the wheels of a departing helicopter. Others point out that the army, upon which the regime is built, remains loyal.

India is concerned. This week its special envoy, Karan Singh, arrived to urge compromise: “The last thing we would want is for Nepal to dissolve into chaos because India's vital security interests are involved.” He was well chosen to deal with the king. His wife is a Nepali aristocrat and his father was the last Maharaja of Kashmir. The message he carries is not known but is likely to be uncomfortable for Gyanendra. India once supported constitutional monarchy and democracy in Nepal. Now it speaks only of democracy.

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Hamas and the world

Isolated, in its violent corner

Apr 20th 2006 | GAZA AND RAMALLAH
From The Economist print edition

AFP

A defiant Hamas defends this week's suicide-bombing in Tel Aviv, despite economic pressure from America and Europe

SUICIDE-BOMBINGS are always shocking, but the young man, Sami Hammad, who took nine lives along with his own on a crowded Tel Aviv street on April 17th will have particularly unnerved Israelis. He came from the northern West Bank, the first area to be fenced off by Israel's separation barrier. Travel between it and other parts of the West Bank, where the barrier is incomplete, is these days highly restricted. The Israeli army had been conducting searches and sweeps in nearby towns, arresting dozens of would-be terrorists. And it had tightened security even more for the Passover holiday.

The bomber showed that there will always be holes. The timing, especially on the morning of the new Israeli parliament's swearing-in, makes it look like a reprisal for several days of Israeli shelling in Gaza, intended to repress Qassam rocket fire but which killed two Palestinian children last week as well as several militants. In fact, the timing was probably accidental. Palestinian Islamic Jihad, which has carried out several bombings despite a ceasefire declared a year ago by militant groups, said it had been making “non-stop efforts” to get another bomber through. Hamas, which runs the Palestinian Authority (PA) and whose militants have largely observed the ceasefire, also called the attack “self-defence” and a “natural result” of continued Israeli depredations.

This has won Hamas a slew of criticisms from foreign leaders. With the PA struggling to pay

salaries as donors turn off the cash, the party's defiant defence of the operation does seem exceptionally self-destructive. But Hamas's attitude has recently been shifting in this direction, in direct response to growing isolation.

Since the party's unexpected election victory in January, the Americans, Europeans, Russians and United Nations have been demanding that it recognise Israel and renounce violence. Policymakers have been debating whether they should cut off funding until the Hamas government either agrees or collapses (America's favoured approach) or whether they should design more subtle ways of encouraging the party to mellow gradually. But with so many countries and so much politics involved, discussions on the more subtle option have come to nothing. The result is that aid and official contacts are gradually being ended by default.

Even Arab leaders, reluctant to sour their relations with America and worried about the example that a successful, democratically elected Islamist government would set for their own autocratic regimes, have been grudging in their support. Recent pledges from Saudi Arabia, Qatar, Iran (and Russia) together come to $202m, six or seven weeks' wages bill.

In the early days after coming to power, Hamas had seemed to be reaching out. It tried to form a national unity government with other Palestinian parties, and sent out a series of moderate-sounding messages, hinting that, under the right conditions, it might abandon its stated goal of destroying Israel. But since this elicited no international response, Hamas reacted by turning ever more belligerent.

In a speech a few days before the Tel Aviv bombing, Ismail Haniyeh, the prime minister, spoke defiantly to the world and told the Palestinians to prepare for hardship. He also criticised the PA president, Mahmoud Abbas, for a series of decrees that undermine Hamas's responsibilities. Mr Abbas, who is from the ousted and disgraced Fatah party, is juggling three conflicting goals: restoring Fatah's dominance, preventing the PA's meltdown and staving off the isolation of the Palestinian people.

Hamas hopes most Palestinians will blame other countries, and maybe Mr Abbas, for their isolation, rather than holding Hamas or the launchers of Qassam rockets guilty for cutting them off from the world. Certainly, foreign visitors often get asked these days why their governments are punishing Palestinians for their democratic choice. With the PA's huge payroll supporting a large swathe of the population, nobody believes that foreigners are trying to punish Hamas and not the people. If the PA does grind to a halt, the loss of basic services, which no foreign relief effort can replace, could be devastating.

A policeman in Ramallah reckons that if salaries go unpaid, it will not take long for unrest in the ranks to spill over. Fatah politicians may seize on this to provoke factional strife. Impoverishment, violence or both loom in a future that looks bleak for Palestinians, and for Israelis too.

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Iraq

Near the point of no return

Apr 20th 2006 | BAGHDAD
From The Economist print edition

Iraq continues to fight and squabble its way to sectarian disaster

IT WAS just another insurgent attack in Baghdad with two rebels dead, said official statements. But the Iraqi press is portraying the battle that raged in the Sunni suburbs of Adhamiya on April 17th as something different and potentially much more dangerous: a rising by the people in a Sunni area against a mixed force of Shia militiamen and government forces.

According to some reports, insurgent groups went door-to-door, rousing men from their sleep to defend their homes against what was assumed to be one of the death squads that have terrorised Baghdad in recent months. If this was indeed so, the fighting in Adhamiya could point to a merger of insurgent groups with mosque guards, neighbourhood defence committees and other local militias. This, in turn, could be the prelude to the partitioning of Baghdad into sectarian enclaves—and another step closer to full-fledged civil war.

AP

Mr Jaafari points to an exit

The demons unleashed in February by the demolition of a Shia shrine in Samarra show little sign of departing. In response to a series of devastating follow-up bombings, including a triple suicide attack on a Baghdad mosque on April 7th which killed up to 90 people, the Shia are declaring that their only option is to act against the Sunni *takfiri* extremists who consider them to be infidels and therefore valid targets.

The Sunnis, for their part, accuse the Shia-led government of conducting the “ugliest form of ethnic cleansing”, as Adnan al-Dulaimi, head of the main Sunni coalition, said after the Adhamiya fighting. Several times a week at least half a dozen bodies are found bound, shot and dumped. The Ministry of Displacement and Migration estimates that 35,000 people, both Sunni and Shia, fled their homes in the first two weeks of April because of sectarian violence.

Meanwhile, Iraq's main political parties continue to fail to form a national unity government. The main point of contention remains the prime minister, Ibrahim al-Jaafari, whom the Kurds say is not to be trusted, and whom Sunnis, and secular-leaning allies of Iyad Allawi, the former prime minister, also reject. Over the past two weeks, even Mr Jaafari's Shia allies have become increasingly lukewarm. Mr Jaafari himself has now apparently softened his position. On April 20th his Dawa party said that he had asked it to reconsider his nomination.

But his opponents are far from united. They have started to quarrel publicly among themselves, with Mr Allawi's list and the Sunni coalition both laying claim to one of the two vice-presidencies. In one telling exchange, Mr Dulaimi said that Mr Allawi represented neither Shia nor Sunni nor Kurd. His remark suggested that, contrary to everybody's protests, the institution of a Lebanon-style system in which posts are shared out along sectarian lines is probably inevitable.

Iraqi politicians have been claiming for weeks to be within days of breaking the deadlock. In fact, the struggle could go on for some time yet. Neither American pressure nor the reported frustration of the venerated Grand Ayatollah Ali al-Sistani appear to have made much difference. A session of parliament, intended to bring the issue to a head, had been postponed for months.

The problem is that there are simply too many groups chasing key posts. With so much oil money sloshing around, and with the parties accusing each other of forming death squads, there is too much at stake and too little trust for one group to agree to relinquish a post to another.

The absence of a government has paralysed decision-making. The likely effects run from high desertion rates in the nascent Iraqi army (because of unpaid salaries) to delays in infrastructure contracts (that need to be signed to boost oil production) to the melding of militias and security forces. Unless the politicians manage soon to form a cabinet that can begin to address these problems, Iraq may pass beyond the point where it can still function as a unified state, a point that may not be noticed until it is too late.

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Egypt

Broken promises

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From The Economist print edition

But who believed an old autocrat's talk of reform?

BEFORE Egypt's first-ever presidential election last autumn, Hosni Mubarak made lots of promises. The vote would be free and fair, said Egypt's ruler, and, if he won, sweeping reforms would follow. Onerous emergency laws, enforced since he took power in 1981, would be repealed, as would laws restricting freedom of the press, the judiciary and the formation of political parties.

Mr Mubarak handily swept the vote, and his party held on to its traditionally beefy parliamentary majority in later legislative polls. Since then, however, reforms have failed to appear. Egypt, which seemed to be progressing towards more open politics, is instead sliding backwards.

AP

An angered Copt knows whom to blame

In December, Ayman Nour, the distant runner-up in the presidential race, with 7% of the vote, was thrown into jail. The outspoken liberal, a diabetic with two young daughters, is serving a five-year sentence, on charges that he forged documents to found his political party. Mr Nour's supporters believe he is being kept out of politics to clear the field for Gamal, Mr Mubarak's 42-year-old son, who, despite protests to the contrary, is seen as a future presidential contender.

The parliamentary runners-up also face trouble. The Muslim Brotherhood captured 88 seats, a record for the opposition in Egypt, and would certainly have gained more without blunt government obstruction of the polling. Still officially illegal, the group continues to be hounded by serial detention of its activists. Recent arrests have included dozens of student leaders, as well as five publishers sympathetic to the Brotherhood, who were rounded up in advance of voting in a publishers' trade organisation.

Oddly enough, the regime has also squashed opposition parties with far less organisational strength or popular appeal than the Brotherhood. Earlier this month, a state-appointed court rejected applications to form political parties filed by mild Islamists and by secular Arab nationalists. Many observers blame government manipulation for the bitter leadership struggle that has crippled the Wafd Party, a traditional voice for liberal secularism. On April 1st, followers of one faction stormed the party headquarters, sparking a shoot-out. Several dozen were injured.

The opposition's weakness has led many reform-minded Egyptians to pin hopes on more narrowly focused pressure groups from outside the formal political system. Several such groups have

emerged in recent years, including unions of university teachers protesting against the interference of security agencies in academia, and journalists demanding an end to the imposition of harsh prison terms for libel.

Despite constant coercion from the ministry of justice, Egypt's 9,000 judges are pressing for the adoption of a law establishing full judicial independence. Having stalled on the issue for over a decade, the ministry recently ordered two of the country's most senior judges to appear before a disciplinary board. Although no formal charges have been aired, the pair's apparent crime is to have protested against blatant, government-sponsored fraud during the parliamentary elections, which were ostensibly monitored by the judiciary. Activist judges have vowed to stage protests until their colleagues are exonerated and their independence guaranteed.

Perhaps the most promising of Mr Mubarak's pre-election promises, for ordinary Egyptians, was the one to abolish the emergency laws. Despite government claims that these rules target only terrorists and drug-runners, the right of arbitrary arrest has been exercised far more widely, creating a general public fear of crossing the authorities. But this week Mr Mubarak hinted that the laws will remain in force, because the drafting of less sweeping anti-terrorism legislation could take as long as two years.

Egyptians must remember that they live in an inflamed region, said Mr Mubarak. “We have to appreciate that Egypt, from time to time, is targeted,” he explained, in an apparent suggestion that recent sectarian strife in the port city of Alexandria, where two people were killed, may have resulted from foreign meddling.

Yet, judging from comments on the rioting, by Coptic Christians angered at a knife-wielding Muslim's attack on several churches, a growing number of Egyptians reject blaming such signs of distress on outside forces. Instead, they blame the regime itself, for placing its own security ahead of its citizens', for failing to uphold the rule of law, and for stifling the kind of public debate needed to address such entrenched problems as relations between religion and the state, between sects, and between rulers and those they rule.

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Iran's nuclear progress

What's in a boast?

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Filling in the gaps in Iran's nuclear story

IRAN'S president is not above poking a finger in the eye of those wanting to contain his country's nuclear ambitions. But it is not Mahmoud Ahmadinejad's proud boast last week—that having successfully enriched a small quantity of uranium in a cascade of fast-spinning centrifuge machines at Natanz, Iran has joined the "nuclear countries"—which most troubles nuclear inspectors (it had almost reached that point before). Rather, by claiming that Iran has more advanced "P-2" centrifuges too, Mr Ahmadinejad has fuelled suspicion that it is still hiding nuclear work. If it is, then guesses by America and others that it might be five to ten years before Iran could lay its hands on a bomb may be astray.

Iran says it wants to produce only low-enriched uranium (last week's was 3.5% enriched) for use in power reactors, not the 90%-enriched stuff needed for most bomb designs. But ever since Iran's long-concealed nuclear work was exposed by regime opponents in 2002, inspectors from the International Atomic Energy Agency, the UN's nuclear guardian, have suspected that it is still hiding something. Might that be some P-2 centrifuges?

Iranian officials eventually admitted that they had received designs for the more efficient P-2s in 1995, from the same Pakistan-centred black-market network that provided the less capable P-1 machines which produced the uranium Mr Ahmadinejad was waving about gleefully last week. But the plans, they claim, were ignored until 2002, when an Iranian company was given the job of conducting tests using some locally produced parts.

The inspectors never bought that story: testing would not have been possible, they worried, without more time to work on the designs. To add to their suspicions, some traces of low-enriched uranium found in Iran have yet to be explained, and may indicate more enrichment work than has been owned up to. Meanwhile, before inspectors could get there, Iran razed a site at Lavizan where nuclear work may have taken place. More recently, a key member of the black-market network, in custody in Malaysia, alleged that Iran bought equipment, not just designs, for the more advanced centrifuges, despite its denials.

Concerns have intensified since Mr Ahmadinejad's claim that Iran has resumed "research" on P-2S. Once it is able to build the new models in some number (no one knows if it yet has all the parts to do so), it will be able to build up its uranium stocks much more quickly than first thought. Experts calculate that it would need about 1,500 P-1 centrifuges, configured to produce highly enriched uranium rather than the civilian sort, to produce enough fissile material for a bomb a year. The P-2S could do that job in half the time.

But might the gaps and evasions in Iran's nuclear story point to a still more worrying conclusion? Some have long suspected that it has a parallel military enrichment programme. Inspectors have uncovered no evidence of that. But a small centrifuge plant would be difficult to detect. Using

hidden P-2 machines, and either starting from scratch or with already partially enriched uranium (getting to 3-5% is already the hardest part) from its publicly known enrichment plant, Iran could spring a much nastier nuclear surprise.

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South Africa

The shower method

Apr 20th 2006 | JOHANNESBURG
From The Economist print edition

Sex and politics collide in a trial that has outraged many South Africans

Get article background

THE first trial of Jacob Zuma, South Africa's former deputy president until he was sacked last June, is coming to an end. A 31-year-old HIV-positive woman accused him of raping her at his Johannesburg home, and a verdict on this charge is expected early next month. This is only the first hurdle he has to clear to be rehabilitated politically; he then faces another trial, for corruption, in July. But even if he is acquitted of those charges, he may already have done himself too much damage with his testimony in this first trial to ever make a comeback. Or at least, he should have done.

Reuters

The eager-to-please Mr Zuma

Mr Zuma's supporters have mounted a vigil in front of the court building for the duration of his trial, chanting for their champion and hurling verbal abuse at his accuser. His easy, back-slapping style, often contrasted with the more aloof manner of President Thabo Mbeki, has won him many backers. But the roots of his popularity go deeper than personality. In spite of the country's good macro-economic performance, unemployment and poverty remain widespread, and many people feel left behind by the government's economic policies. Some in the ruling African National Congress (ANC) party resent what they see as a centralisation of decision-making, while the party's trade-union and communist allies feel increasingly sidelined as well. Mr Zuma and his rural Zulu roots also appeal to traditional segments of society. These disparate groups have all pinned their hopes for a change of course on him.

Indeed, Mr Zuma's more ardent supporters claim that these court cases are just part of a complex political conspiracy to prevent him from succeeding Mr Mbeki, due to step down in 2009. Mr Zuma's defence team has tried to undermine the credibility of his accuser—who is alleged to have made false rape claims in the past—and he may well walk free. If he is also cleared of corruption in time for the ANC congress next year, then it remains possible that he could still gain support as the party's next presidential candidate.

That would be a mistake. Mr Zuma's performance in court so far raises fundamental questions about his suitability for further political office, let alone the presidency. He has admitted having unprotected sex with his accuser—although he maintains it was consensual—in spite of knowing she was HIV-positive. Though he once headed the country's official anti-AIDS campaign, he also explained that he took a shower immediately after sex to “minimise” the risk of infection.

AIDS activists argue that this sort of talk could seriously undermine efforts to contain the pandemic and to debunk the many myths surrounding the disease. South Africa has one of the highest HIV-infection rates in the world. HIV/AIDS help-lines now have to explain to confused callers that showering is not the preferred way to avoid catching the disease.

Mr Zuma's trial has also highlighted the fragility of women's rights in a country with one of the highest incidences of rape in the world. Some of his followers have supported him with such felicitous slogans as “burn the bitch”. This has provoked outrage from women's groups—but not a peep from Mr Zuma himself.

The former deputy president, who testified in Zulu, maintains that his accuser seduced him, pointing out that she came to his house wearing a skirt. According to his Zulu culture, he claims, leaving a woman in a state of sexual arousal is unacceptable, and he had to oblige. All this flies brazenly in the face of South Africa's carefully nurtured official policy on women's rights, reflected in the constitution and—officially—promoted assiduously by the ANC.

South Africa needs political leaders capable of tackling the double scourge of HIV/AIDS and violence against women, which have blighted its post-apartheid renaissance. Mr Zuma may survive his days in court, but has surely proved in the course of his own defence that he is not and cannot become one of them.

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Chad

The French connection

Apr 20th 2006
From The Economist print edition

Chad's president clings to power, with the help of some powerful friends

IT WAS a very African story. On April 13th, hundreds of rebel troops advanced towards Ndjamena, the capital of Chad, intent on unseating President Idriss Déby. After months of escalating violence, the conflict between Mr Déby and his enemies seemed about to reach its bloody *dénouement*.

But the rebel column had been tracked by troops from the former colonial power, France, which was standing by their man. The French, who maintain 1,300 troops in Chad, fired warning shots over the column. Not to engage the rebels, says one French officer, but to "articulate" France's position. The rebel attack faltered, its soldiers shot down on the steps of the parliament, and at least a hundred were killed.

Most of Mr Déby's anger over the failed coup has been directed at neighbouring Sudan. Many of the rebel groups operate out of the Darfur region of Sudan, abutting western Chad. A proxy war between Sudan and Chad has been simmering for a while. At least some of the Chadian rebels are thought to receive Sudanese backing, and some Sudanese rebels contributing to the violence in Darfur receive Chadian support. Mr Déby has now broken off diplomatic relations with Khartoum completely.

He also threatened to expel the 200,000 Sudanese refugees from the conflict in Darfur who now live in camps inside the Chadian border, before being talked out of it by the UN. Mr Déby has relented slightly on another threat, to halt oil production over a dispute with the World Bank on how Chad's oil revenues should be spent. The Chadian government, accepting American mediation, has now given the oil-producing consortium that produces the oil and the World Bank until the end of the month to pay the $125m it feels it is owed, to spend in any way it sees fit. The World Bank, which helped to bankroll an oil pipeline in Chad, says that the oil money should only go to improving schools and clinics, as was originally agreed with the Chadian government.

Meanwhile, Mr Déby promises that the presidential election will go ahead as planned on May 3rd, despite a possible boycott by the opposition parties. They object to the president having changed the law to allow him to run for what will be his third term of office. Even if Mr Déby gets his oil money, it is unlikely that he will do very much to alleviate the poverty and sporadic violence that has scarred Chad during the 16 years of his rule.

But Mr Déby is likely to hang on, largely due to the French. With Mr Déby so weak now, their

forces are the only element capable of preventing the country from slipping into chaos. The French have probably calculated that however ineffective and authoritarian Mr Déby may be, the alternative could be much worse, causing thousands of deaths in Chad and making the grim situation in Darfur even worse.

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Correction: Omar Abdel Razeq

Apr 20th 2006
From The Economist print edition

Omar Abdel Razeq, the Palestinian finance minister, was a graduate of Iowa State University not, as we said on April 1st (see article), the University of Iowa. Our apologies.

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Great powers in the Middle East

Russia is not a piece of furniture

Apr 20th 2006 | MOSCOW
From The Economist print edition

Kremlin watchers wonder what Vladimir Putin is up to with Hamas and Iran

A LONG wait for a meeting at a Russian naval base was enlivened recently by a curious overheard conversation. A retired Russian officer said he was trying to claim a financial allowance due for combat service rendered in Soviet times. Where was it? In the 1980s, he said, off the coast of Lebanon. At that time, the Middle East was one of the main arenas for proxy cold-war confrontation. And it increasingly seems to be the region selected by Russia for a renewed tussle for influence with its old rival.

This week, Russia re-stated the positions that, to America's discomfort, it has staked out on two combustible regional issues: how to deal with Hamas—victors in January's Palestinian election—and how to handle Iran. At a diplomatic powwow in Moscow, the Russians reiterated their opposition to the use of either force or sanctions to deter Iran's nuclear ambitions. Meanwhile, Russia agreed to provide the Hamas-led Palestinian Authority (PA) with financial aid—America and the European Union having suspended theirs—this week's suicide bombing in Tel Aviv notwithstanding.

On the face of it, Russia's dalliance with Hamas, and patience with Iran, look odd, given Russia's own experience of Islamist terrorism, Iran's proximity to Russia's volatile north Caucasus, and the valuable role Russia enjoys as the region's sole official nuclear power. Dmitri Peskov, a Kremlin spokesman, insists that Russia's sensitivity on Iran is equal to America's.

But look closely, and their interests arguably differ. To the Kremlin, Iran has been a well-behaved neighbour, which has kept out of Chechnya, and the Russians want to keep it that way. Russia is less anxious than America about Israel's security. Dimitri Simes, of the Nixon Center in

Washington, says a nuclear Pakistan, which America regards as an ally, is a bigger worry in Moscow than is Iran. Cash is also at stake: Russia is helping to build a nuclear plant for the Iranians. Last year it promised them a batch of ground-to-air missiles—though they have yet to be delivered, and won't be, if the Americans get their way.

More important than these concerns, however, may be another, uniquely Russian kind of interest. Dmitri Trenin, of the Moscow Carnegie Centre, says the Kremlin's aim in the Middle East is to show that “Russia is not a piece of furniture.” Or, as one American administration official puts it, the message is, “We're back.” Oil at $70 a barrel, he says, has inculcated “a self-confidence [in Moscow] that we haven't seen since the break-up of the Soviet Union”. To prove it is not a piece of furniture, Russia needs to do something visibly different from America. And as Georgy Mirsky, a Moscow-based analyst, argues, for one reason or another the Middle East is the best place for Russia to do it.

This new imperative seems the best explanation for the invitation issued by Vladimir Putin, Russia's president, for the leaders of Hamas to visit Moscow, which they did last month. The public rationale is that Hamas won a democratic election; that dialogue is better than isolation; and, moreover, that Russia has not officially designated Hamas a terrorist group, as other governments have: perhaps it can be converted to peaceful politics, as was the Irish Republican Army.

Yevgeny Primakov, an ex-prime and foreign minister still thought to wield influence, says its historically good relations with the Palestinians, Syrians and others give Russia “special opportunities” in the Middle East. Mr Primakov says he is sure the Hamas initiative was quietly agreed with America and other parties, even though they squawked in public.

Actually, says that American official, “we were very, very unhappy.” The decision to fund the Hamas-led PA has taken Russia even further from the previously agreed line. The Hamas poll win—a “great blow” to American policy, crowed Mr Putin—seems to have created a perfect, if temporary, match. As Avinoam Idan, formerly an Israeli diplomat in Moscow, puts it, Hamas was looking for recognition; the Kremlin was looking for a chance to demonstrate its independence.

And rather than the considered wiliness for which Mr Primakov was once renowned, the Hamas invitation announced by Mr Putin looks like evidence of a different trend: the Kremlin's tightening grip on policymaking. Americans say that Russia's foreign ministry was as surprised by the move as they were. Divining who in the Kremlin has the president's ear is tricky; but among them, says Mr Mirsky, are some who are schooled to befriend “any thug in the world who declared himself anti-American”.

There are some, says Mr Simes, who feel Mr Putin and his predecessor, Boris Yeltsin, were too obliging to America over Kosovo, Iraq and America's incursions in Central Asia. Many top officials regard America's promotion of pro-western forces in the former Soviet states as a provocation, and the stalling of Russian efforts to join the World Trade Organisation as deliberate American sabotage.

Russians become doubly suspicious when they see signs of a link, however tenuous, between America's cultivation of new friends in the ex-Soviet world, and its broader Middle East policy—take, for example, the fact that Georgia recently raised its contribution to the American-led coalition in Iraq. “We want to be contributors as well as consumers of security, and the Russians scold us for this,” says Nino Burjanadze, Georgia's parliamentary speaker.

For the Russians, there is a risk that their new foreign policy may prove as counter-productive as Kremlin-run economic policy has sometimes appeared to be. Still, so far, the strategy of irking and embarrassing America in the Middle East, without risking a serious rupture, is holding up. Despite some pressure in Washington for George Bush to “punish” Mr Putin for his policies, domestic and

foreign, there is little will in his administration to give Russia any more than an occasional rebuke.

Iran may change that. The gap between the American and Russian positions has narrowed: the two countries, says that American official, are at least now reading from the same book, if not the same page. But as Iran has ascended the list of American preoccupations, the importance of the gap has grown. In the end, the Kremlin may have to weigh the risk of serious American displeasure, and of a nuclear Iran, against the value of its newly prized autonomy. Tactical incentives from Washington, perhaps over the World Trade Organisation, may help.

In some Russian behaviour, national and personal interests (including the financial kind) are hard to disentangle. That may be the key to a strange tale that emerged recently of the intelligence alleged (by the Pentagon) to have been leaked by Russians to the Iraqis before and during the war of 2003 (the Kremlin denies it). Just as mysterious was the apparent pre-war trip to Baghdad of two hard-line, retired Russian generals, and the convoy of people, documents and who knows what else, from Baghdad to Syria, said to have been led by Russia's ambassador.

The Americans seem less perturbed about all that than might have been expected. Perhaps they concluded that the implicated officials were acting alone, or consoled themselves that, whatever the Russians got up to, it made little difference in the end. Or perhaps they decided their dance with the Kremlin in the Middle East was delicate enough, without restarting old arguments.

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For the second year running, the Danube surges in spring

Dam that water

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From The Economist print edition

EPA

A dinghy proved to be the only practical way to get round Nikopol in Bulgaria. It was among scores of towns and villages all over south-eastern Europe that were inundated as the Danube surged to levels not seen for 100 years. Europe's second-largest river has been swollen by torrential rain and melting snow. In Romania, people hunkered down in schools and hospitals, sometimes bringing their poultry and livestock with them, as rescue workers struggled to repair breached dams.

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New Germans

Multicultural hysterics

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The harsh reality of immigrants who can't or won't fit in

HYSTERIA has its roots in personal issues which are long-suppressed and unresolved, said Sigmund Freud, whose 150th birthday (on May 6th) will be widely commemorated in the German-speaking world. Even if Freud's ideas seem simplistic today, they may help to explain the German penchant for getting into a tizzy over long-standing, half-hidden problems that suddenly seem impossible to escape.

Take Germany's school system, whose inefficiency and social injustice have been an open secret for decades. When, in 2001, an OECD study actually spelled out that unpleasant truth, it put the entire country in a state of shock.

In another encounter with harsh, partially suppressed reality, the Germans have just woken up to the fact that they face big problems with the social integration of immigrants. This time, the wake-up call was a letter from the teachers of the Rütli school in Berlin, whose pupils are mainly Turkish and Arab. Close our school, they begged, because our students are so violent that teaching has become all but impossible. The debate has been sharpened by last week's guilty verdict on a young Turk who killed his sister after she “dishonoured” her family with her western lifestyle.

Hardly a day now passes without a new proposal to address the cultural and social problem of integrating migrants. On the left, people want to get rid of the Hauptschule, the bottom layer of a widespread selective secondary school system. On the right, there have been calls to punish youths whose behaviour shows they are not willing to integrate—by expelling them from school or even sending them to a “taster jail”. Chancellor Angela Merkel will soon convene an “integration summit” to air these and other ideas.

For outsiders, it is hard to understand the fuss. Compared with France and Denmark, Germany wouldn't appear to have much of a problem with its immigrants, particularly in view of their large numbers. The country's residents include 6.7m holders of foreign passports, making up 8% of the population. Then there are 7m German citizens classed as having a “migrant background”—this includes the children of mixed or immigrant parents and ethnic Germans who have come from eastern Europe (mostly knowing no German). Yet there are few slums comparable to France's *banlieues*;and during the “cartoon wars” in February, Germany was an island of relative calm.

Still, it would be wrong to call integration in Germany a success. Youngsters with foreign roots have difficulty finding a niche in society—in large part because of flawed immigration, education and labour-market policies. More than other European countries, post-war Germany attracted low-skilled immigrants—many of them “guest workers”, who were expected to go home one day. Many Turks, in particular, never did. This has left Germany with a large cohort of “second-generation” immigrants with origins in poor parts of Turkey and little hope of social or educational success.

Often speaking German badly, it is Turkish boys, especially, who end up in the Hauptschule. Even if they do finish school and get vocational training (40% do not), they have a hard time finding a job. At 26%, unemployment among immigrants is more than twice the national average.

Add in demography, culture and religion and it is easy to see why things may get worse before they get better. Youths with a migrant background will soon outnumber native Germans in some big cities. Feeling rejected by mainstream society, many resort to violence or stay in ethnic ghettos. Some feel attracted by Islamist organisations, which have been growing of late, albeit very slowly.

Although much of this was predictable, the very issue of integration has long been a taboo subject, says Klaus Bade of the Institute for Migration Research and Intercultural Studies at Osnabrück University.

Still yearning for cultural homogeneity, conservatives refused to accept that Germany was a country of immigration. Some on the left were also in denial: they rejected anything that smacked of putting pressure on immigrants to integrate, seeing such talk as an echo of fascism. Meanwhile some politicians play to the gallery; in a sop to nativist sentiment, the governments of the states of Hesse and Baden-Württemberg developed “naturalisation tests” with questions on culture and politics.

Unsurprisingly, polls show that immigrants do not feel welcome. More worryingly, according to a study by Bielefeld University, Germans seem to be increasingly xenophobic: 61% agree that “there are too many foreigners living in Germany”, compared with 55% in 2002. And racial violence is rising again. This week, an Ethiopian scientist with a German passport was almost beaten to death.

Still, there are signs that Germany is inching toward a more realistic approach. Although flawed in some ways, a new immigration law is the first to accept the need for active measures to promote integration, albeit only through language classes. And even some conservative state governments have launched decent integration plans. The state of North Rhine-Westphalia, for instance, governed by a coalition led by the right-of-centre Christian Democrats, now boasts an “integration minister”, Armin Laschet, who berates his own party for being late to recognise reality.

The integration summit, due to be held before the summer break, could mark another step forward. Yet to make a real difference, says Mr Bade, the meeting must generate some smart thinking on how to ensure equal opportunities for people with an immigrant background, particularly the young. Above all, he says, they need more teachers, smaller classes and schools that operate for longer hours.

Such action will take time to work, of course. An even harder task will be to convince Germans that immigration need not hurt them. It will take brave and imaginative politicians to persuade the nation that it may need to take in even more foreigners, given its demographic profile and the global competition for talent.

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French protest

Starved into surrender

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A pre-emptive strike by a politician from the Pyrenees

IF IT takes 3m French street protesters to overturn a law, how many does it take to stop a factory relocating? Answer: one—but he has to be a member of parliament and on hunger strike. This form of protest, it would seem, is the latest weapon in France's battle to protect jobs. On April 14th Jean Lassalle, a deputy for the centrist UDF party for the Pyrenees and the son of a mountain shepherd, ended a hunger strike after 39 days—and the loss of 21 kilos (46lb)—when a Japanese company agreed to reinvest in his Pyrenean valley.

Mr Lassalle began his fast in March, sitting almost daily on a sofa in an ornate room of the National Assembly in Paris, to protest against what he considered to be a relocation plan by Toyal, a Japanese-owned manufacturer of aluminium pigment. The company's French plant employs 150 people in the Aspe Valley, near the Franco-Spanish border, home to some 3,000 inhabitants and birthplace of Mr Lassalle. It had plans to add a second factory in Lacq, some 70 kilometres (44 miles) north. Toyal's bosses said that they were expanding, not moving away, and would not shut the Aspe Valley plant. Mr Lassalle disbelieved them, arguing that it was a prelude to closure, and began his fast.

Reuters

A new sort of belt-tightening

For weeks, the thinning Pyrenean deputy in the parliament building attracted little attention. But as his health deteriorated, his fate swiftly became an affair of state. Late last week, Dominique de Villepin, the prime minister, paid him a surprise visit. President Jacques Chirac telephoned him to assure him that the affair would be resolved. As Mr Lassalle was hospitalised in an emergency, Nicolas Sarkozy, the interior minister, signed an agreement with Toyal: the Japanese firm would expand within Mr Lassalle's Aspe Valley after all, and the French government vowed to compensate it for any extra costs that might be involved in abandoning the site at Lacq.

Mr Lassalle appears to be recovering: this week he ate a little fish and green beans, and grumbled amiably that the doctors wouldn't allow him a glass of red wine. The French, meanwhile, are digesting the affair in various different ways. For some, it was a noble Gallic victory against the brutal forces of capitalism. François Bayrou, UDF leader, saluted “the heroism and the sacrifice” of the Pyrenean deputy, “a man alone against the extraordinary economic and financial power of many multinational companies”. For others, it testified to France's institutional failings. It was a “sign of bankruptcy, the symptom of the sickness of our political system”, said Noël Mamère, a Green deputy. For others still, it was simply blackmail. In the terse words of Japan's ambassador in Paris, Hiroshi Hirabayashi: “Japanese investors will hesitate to settle here, for fear of being held hostage.”

Charlemagne

Ducking change, the European way

Apr 20th 2006
From The Economist print edition

In a turbulent world, Euro-voters should live a bit more dangerously

“WHAT do you expect from life—full coverage against all possible risks?” Yes, seems to be the Europeans' reply, just as it was Philip Marlowe's when he was mockingly asked that question at the end of Raymond Chandler's “The Long Goodbye”.

From the Italian and German elections, to French students marching against labour reform, back to the rejection of the proposed European constitution last summer, the constant theme of continental Europe during the past year has not been the triumph of the left (otherwise Christian Democrats would not have won in Germany), nor support for economic nationalism (which the Italian and German governments say they oppose, unlike the French one). It has been the minimising of change, even the kind that should, in theory, come easily when a government has a clear mandate. Risk aversion, it seems, has become the defining feature of political behaviour in continental Europe's largest countries.

Europeans have always been more risk-averse than Americans. This manifests itself in many small ways. German bankruptcy laws, for example, can ban entrepreneurial businessmen from operating a company for decades if their gambles backfire, while in corporate America, you are nobody until you have been made bankrupt a couple of times. In France, a poll found that an amazing three-quarters of the young would happily work as civil servants.

Risk aversion manifests itself in large ways, too. Europe's comprehensive welfare systems are grand insurance policies against the risk of falling ill, losing your job, or declining into poverty. The American system rewards risk-taking. Europeans think it is better to be safe than sorry.

At the moment, Europe seems to be even more risk-averse than usual. The reason is clear: risk aversion is a product of economic uncertainty, which is growing. Greater competition in goods markets, plus trade liberalisation plus outsourcing plus globalisation all add up to a more turbulent economic environment. People fear that jobs are being destroyed faster than they used to be (this is not true, but people think it is). Older workers, especially, fret that they will not have the specific skills needed to do the new jobs that are created. And if the voters are nervous about change, it is hard to lay the blame on politicians for reflecting their mood—though one can perhaps fault them for hiding the true costs of not changing and for pretending the current system can go on longer than it actually can. In this way, risk aversion feeds on itself.

But it also has growing, and damaging consequences. In modern economies, people are constantly moving in and out of jobs, and the rate is surprisingly high: some 4% of jobs change hands each month in France. You would expect that if uncertainty really were increasing as much as opponents of globalisation say it is, then this rate of “churning” would have risen lately. In fact, the opposite is happening. Jobs are being created and destroyed slightly more slowly than they were in 1970.

The best explanation is the combination of high unemployment and labour laws that protect against being fired. Unemployment makes it harder for an employee to go out and find a new job. Labour laws increase the employer's cost of hiring someone new. So there is less movement into and out of jobs. This hurts the whole economy, not just the individual worker or company. As Olivier Blanchard, France's most distinguished economist, puts it: “modern economies need to constantly reallocate resources including labour from old to new products, from bad to good firms.” Risk aversion increases labour-market rigidities and slows this process down.

It also helps explain the uncompromising, sometimes hysterical nature of opposition to any kind of change. As Mr Blanchard says, there is a conflict between workers who value security and the economy as a whole, which needs flexibility. But this conflict does not have to be damaging, and is not all that hard to resolve. In essence, the point is to protect workers, rather than jobs. This is what successful European countries do, such as Denmark or the Netherlands (which by OECD measures have lower unemployment rates than America). It does not imply the dismantling of the welfare state, which is why Europe's economic problems are not quite as ruinously insoluble as they sometimes seem.

When privilege looks precarious

But in big continental countries, the power of “insiders” is making this solution harder to adopt. Insiders—people with jobs in the public sector, or with secure private-sector employment—see economic reform not as a particular set of proposals, to be judged on its merits, but as the thin end of a wedge that threatens their whole privileged status. To them, the possible gains from change are worth less than the risk of losing what they already have—the definition of risk aversion. This makes current insiders determined to reject reform almost across the board, and provides those who hope to be insiders in future—like French students—with an incentive to support the system as it is, rather than change it. Theirs is a logical choice. But as a result, large continental economies are becoming locked into opposing small changes which might benefit people and which they might even support in the abstract.

Risk does not go away because you are averse to it; trying to make yourself invulnerable to small risks can end up leaving you more vulnerable to larger ones. You can, to a considerable extent, insulate some, even many, people from the risk of losing jobs, or being forced to work more than 35 hours a week, and so on. But you leave the country as a whole more open to other, more dangerous risks: creating fewer jobs, creating an underclass of people who have never had a job, and seeing your economy bypassed by those willing to take bigger chances than you are.

British carmaking

Peugeot packs its bags

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From The Economist print edition

Another car plant dies; long live British carmaking

AFP

APRIL is the cruellest month for carmakers, it seems. A year and ten days after the collapse of MG Rover, the last of Britain's domestically-owned volume car manufacturers, Peugeot said it too planned to close its assembly plant in the West Midlands, cutting 2,300 jobs by July 2007.

That Ryton, an old factory near Coventry where the now-creaking 206 model is produced, is to close surprises few. Its fate was sealed in 2003 when PSA Peugeot Citroen, Europe's second-biggest carmaker, decided to make the 206's successor in a new factory in Trnava, Slovakia. Even so, the unions called Ryton's demise a “nail in the coffin” of the British car industry, while ministers tripped over each other to express their disappointment.

The real surprise was that Ryton stayed open as long as it did. Production peaked in 2003 at almost 210,000 cars that year. At the time, the plant was running four shifts, seven days a week. By last year it had slumped to fewer than 130,000 cars, two shifts and four working days, as demand for the nine-year-old model fell and it was steadily pitched downmarket. Domestic sales have slipped by some 33% since 2002, to fewer than 70,000 cars last year.

As for the timing, Peugeot's automobile division saw a drop in its revenues in 2005, even though it sold more cars. A sharp narrowing of operating margins doesn't just suggest that a firm is engaging in deep discounting in order to keep moving cars; it also begs for excess capacity to be culled. But British unions are voicing two widely-held suspicions over the decision to close Ryton rather than a French plant that also produces the model.

The first is that national ownership of companies does matter, and that Ryton was singled out because Peugeot would have faced greater political heat had it closed a factory back home. The second is that Britain's flexible labour market makes it easier and cheaper to fire workers than do France's more restrictive laws.

There is some truth to the claims. Consulting with trade unions and negotiating job cuts in Britain takes about three months. Doing the same in France takes up to a year, and companies have also to convince officials that jobs must go in the first place. Overall, it costs two or three times more to trim a job in France than it does in Britain, says William Dawson, of Simmons & Simmons, a law firm.

And concerns that Peugeot under-invested in the plant for years (knowing that closing it to move production to eastern Europe would be easier than shutting a factory in France) are gaining wider resonance as ever more British manufacturers are bought by foreign firms. “It would be difficult for a French manufacturer to leave their home market because it is their home market,” says Thomas Ryard, of Global Insight, which tracks industry data. “Britain's problem is that there is no national pride in keeping production in the UK.”

Nonetheless, Peugeot has cut a shift at the two plants in France that make the 206, eliminating about 1,500 jobs. And it has several pressing reasons for closing Ryton.

The first is logistics. Each car made at Ryton costs about €400 ($490) more than similar cars produced in France, says Jean-Martin Folz, the company's chief executive. That is not because British workers are any less productive: at its peak, Ryton produced 63 vehicles per employee a year, just three fewer than Peugeot's factory in Mulhouse and more than the 56 notched up by Poissy, another French plant, according to Global Insight.

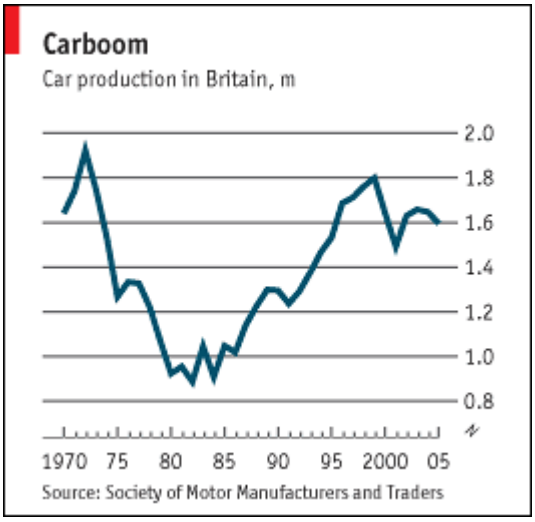
More than €200 of the difference comes from the cost of shipping engines and other components from factories in continental Europe to Ryton, which imports 75% of the parts it needs. Although a strong pound and weak euro may have encouraged Ryton to keep importing parts from outside, the practice sets it apart from most other volume carmakers in Britain. Together, they produce more than 3m engines, almost twice as many as the 1.6m cars they assemble.

The second reason is Ryton's age. It started life making aeroplane engines in the second world war and would have needed an investment of €255m to modernise now (the British government offered a grant of £14m, or €20m). Japanese rivals in Britain, meanwhile, are building cars in brand-new factories built to house the latest production techniques. And while Ryton makes just a single model, Peugeot's French plants produce at least two, many of which share components to cut costs.

Yet, Peugeot apart, British car manufacturing is flourishing these days (see chart). Last year Britain exported 1.2m cars, a record. BMW is investing £100m ($179m) to make more Minis in Oxford. Toyota has added capacity at its British factory, while Nissan's British production may rise to 400,000 cars next year from 315,000.

But that is where the good news ends. Many industry experts believe that BMW's car plant in Leipzig, opened last year, will be the last big car-assembly plant that is built in western Europe. Significant new capacity will probably be added only in low-cost economies in eastern Europe or in developing countries such as China and Brazil. So the bigger question now is whether existing plants—not just in Britain, but in western Europe as a whole—will be able to compete with factories elsewhere

for the investment needed to introduce new models and sustain existing jobs. Peugeot's decision to shift production to eastern Europe may well be a sign that Britain's carmaking renaissance will prove to be short-lived.



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Nuclear energy

Power politics

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Critics of Tony Blair's plans for a nuclear revival make their case

Get article background

AFTER 25 years in the political wilderness, nuclear power is back in favour in Britain. A combination of dwindling fossil-fuel stocks in the North Sea, rising greenhouse-gas emissions and a high oil price pushed Tony Blair into launching an energy review last year to re-examine an issue that his government last looked at as recently as 2003. Most observers think the review is designed merely to rubber-stamp a nuclear revival that the prime minister has already decided on in private.

Support is far from universal. In the past month, two influential bodies have produced reports arguing against a renewal of nuclear power. Last month it was the Sustainable Development Commission, an independent outfit created to advise the government on greenery. Over the Easter weekend, the Environmental Audit Committee (EAC), a parliamentary body, weighed in with its own criticisms.

The committee's first worry is the time it takes to build nuclear-power generators. Around a quarter of Britain's generating capacity is due to disappear over the next ten years, as elderly nuclear plants are decommissioned and new environmental rules make coal stations more expensive to run. The MPs argue that, given the long lead time on new nuclear plants, they could not begin to make a contribution until 2019. That would be too late to bridge the likely generation gap.

Their next worry is that support for atom-splitting might, in the meantime, mean less help for other low-carbon technologies like wind and wave power, or carbon capture and storage. That could leave Britain dangerously reliant on imported gas for much of its electricity supply.

Such crowding-out is inevitable, say the MPs, because nuclear power would require big subsidies to make it attractive to investors. That is because nuclear power plants—which have high initial capital costs and take a long time to start up and shut down—are risky in Britain's volatile, privatised electricity markets, which favour cheaper, nimbler technology (such as gas generation) better able to meet rapid changes in demand. A long period of cheap power could cripple a nuclear operator, as British Energy (which owns Britain's newer nuclear plants) found when the government was forced to bail it out in 2003. The EAC cites a study by Oxera, an economics consultancy, which estimated that at least £1.6 billion ($2.9 billion) of public money might be needed to ensure 8GW of new investment and replace the losses from decommissioning old reactors.

The costs of nuclear power extend far beyond a reactor's operating life, too. The Nuclear Decommissioning Authority, set up last year to dismantle Britain's nuclear power stations, now

reckons that the total cost to the taxpayer of running down, decommissioning and cleaning up Britain's civil nuclear sites will be around £70 billion over the next century—up from its initial guess of £56 billion.

But not everyone agrees that atomic energy requires public money. Ministers say they remain committed to liberalised markets and insist that new reactors will have to be privately financed. William Vereker of Lehman Brothers, an investment bank, argues that financial markets will take the risk of building, running and decommissioning new nuclear plants so long as the state provides non-monetary support in a few areas—such as expediting planning applications (the planning process for Sizewell B, Britain's last nuclear plant, lasted six years) and deciding what to do with nuclear waste.

A few companies—notably E.ON, a German electricity generator—have expressed tentative interest in building reactors in Britain. Atom aficionados point out that the market is currently rigged in favour of renewable energy sources, since the Renewables Obligation, the government's main subsidy for carbon-free power, does not apply to nuclear energy. Changing that, they argue, would improve the finances of the nuclear option.

Mr Blair might also take heart from polling evidence that suggests the public is warming to a nuclear revival. A MORI poll for the Nuclear Industry Association published in December 2005 found 41% in favour of building more reactors to replace existing ones, up from 35% a year before.

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Scotland's nuclear debate

Fission

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A split threatens the ruling coalition

Get article background

A ROW over nuclear power is widening rifts in the alliance between Labour and Liberal Democrats, who together have ruled Scotland since devolution in 1999. As politicians draft their manifestos for elections to the Scottish Parliament in the spring of 2007, the coalition itself looks at risk.

Echoing the debate elsewhere in Britain, Scotland's pro-nuclear camp argues that the lights could go out if the humming nuclear giants at Hunterston and Torness are not replaced before their planned closures in 2011 and 2023. Between them, the two sites supply 35% of Scottish electricity.

Yet many Scots hate nuclear power. In a recent ICM poll for the BBC, 51% opposed constructing nuclear power stations in Scotland. There is widespread hostility to the nuclear submarine base near Glasgow. Some worry that their country will become a dumping ground for waste if new nuclear power generation is sanctioned. Most of Scotland's six most active parties—including the Liberal Democrats—have lined up with popular opinion.

This is causing problems for the Lib Dems' Labour co-rulers. The parties' nuclear fudge after elections in 2003—that the Scottish Executive would make no decisions until the issue of waste disposal had been dealt with in a report for Westminster this summer—has enabled the Executive to stay neutral.

But the energy question could now prompt seismic shifts in the political landscape. At their spring conference in March, the Lib Dems voted overwhelmingly to oppose a new generation of nuclear plants. Jack McConnell, Scotland's First Minister, says he will wait for the publication of Tony Blair's energy review in June but also talks of blocking any nuclear recommendations it might contain. Yet both his Scottish Labour Party and the Scottish Trades Union Congress, nervous about job losses, backed nuclear power at their recent conferences. Most expect Mr McConnell in time to fall in line with London.

Giddy Lib Dems think they have a chance to unseat Labour next year as the largest party in Scotland. That's unlikely, even if Labour takes the unpopular side of the nuclear debate. In either case, a coalition re-shuffle looks increasingly likely—with a chance that the Scottish Nationalists will emerge as both bigger parties' partner of choice.

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The Queen at 80

Revolution postponed

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Why the monarchy is stronger today than ten years ago

Get article background

FOR most of its history, Britain's monarchy has attracted a healthy amount of criticism and satire. Kings have repeatedly been lampooned as lazy, ineffectual, greedy, vain or stupid. When King George IV, who was thought to possess most of these vices, died in 1830, the *Times* reckoned that "there never was an individual less regretted by his fellow creatures than this deceased king." Yet Queen Elizabeth II, who celebrates her birthday on April 21st, attracts almost no hostility from mainstream politicians or the press, despite being born into a job that is subsidised, extravagant and seems largely pointless. To mark the event, the BBC even broadcast a laudatory documentary showing a hardworking queen busily representing the nation to itself, which is what monarchists argue the institution is for.

Compare the fortunes of the monarchy with those of another established institution with an ambient role, the Church of England, and it becomes clear that the royal family is doing rather well. It has recovered from a Princess Diana-fuelled dip in the late-1990s: polls show that more people now think the monarchy will be around in ten years time. Yet attendance at Church of England services has continued to decline. Why is the queen prospering while the Church (outside its cathedrals and evangelical movement) languishes?

AFP

And what do you do, Ma'am?

One reason is that the monarchy thrives on indifference, while the Church is hurt by it. That might sound odd, given that evidence of interest in the royal family is everywhere: over a million people turned out in London for the queen's golden jubilee; dreary books about royals easily outsell ones about elected politicians; and the young royal princes fill the newspapers. But this fascination does not run very deep. According to one poll, only 10% of people aged between 16 and 24 think the monarchy is important to their lives. But because the royal family is the monopoly provider of a something trivial, it hardly seems worth opposing. The Church, by contrast, offers a vital service to its 1.7m members—spiritual succour—and operates in a competitive confessional market where dissatisfied Christians can shop around. Indifference is thus a threat.

A second reason is that the queen's avoidance of controversy (she never expresses political views) and of the press has reinforced the institution she embodies. She never gives interviews, modelling her media strategy on that of her mother, who gave an interview in 1923 but apparently did not enjoy the experience and kept quiet for the rest of her life. (This was probably wise: Cecil Beaton's diaries describe her as "a marshmallow made on a welding machine".) One executive of a

tabloid newspaper argues that this has enhanced the queen's mystique, comparing her with other celebrities who risk irritating their audience through over-exposure. The Church, on the other hand, cannot avoid damaging controversies even when it wants to, as the divisive row over ordaining gay priests reveals.

Third, the monarchy has benefited from a decline in party allegiance and a dilution of ideology in British politics that has not similarly helped the Church. Vigorous anti-monarchism was associated with the hard left, and has atrophied with it. Britain has only one sizeable anti-monarchy club these days—Republic, which has a thousand members—yet when the Prince of Wales had marital problems in the 1870s, 84 were founded.

Vernon Bogdanor, of Oxford University, argues that the decline of party allegiance has also increased the appeal of a non-partisan head of state. The same is not true for the Church. While the Conservative Party had 2.5m members (as it did at its peak), the notion that the Church was the Tory party at prayer did not imply empty pews. Now the Conservatives have only around 250,000 members, it does. Game, set and match to the Windsors.

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City academies

Glass palaces, political stones

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The threat to Mr Blair's cherished education reforms

EASTER week was hard on city academies, Tony Blair's pet programme to redeem failing schools in poor neighbourhoods. On April 13th Des Smith, a head-teacher in East London and former council member of the Specialist Schools and Academies Trust (SSAT), was arrested in connection with Scotland Yard's investigation into the alleged sale of peerages. Four days later, the National Union of Teachers voted for a country-wide campaign against academies. Then on April 19th the National Association of School Governors asked that the programme be halted.

City academies were started four years ago in an attempt to replace appalling secondary schools with better ones. The semi-independent institutions are run by sponsors, who stump up a maximum of £2m; the remaining 90% of their budgets comes from the state. Sponsors have control of the governing body and some power over admissions, dealing with bad behaviour and the contents of the curriculum. Academies need not hire staff registered with the General Teaching Council, as other state schools do, and they can opt out of national pay agreements.

The government wants to see 200 city academies in operation by 2010, up from 27 at present. Are children learning more at them? It is still early days, but figures from the Department for Education and Skills (DfES) show that the number of academy pupils who get good GCSE results is improving at a rate three times the national average. A report to be published next week by the SSAT will show that all specialist schools taken together actually outperform other state secondary schools.

Critics are not convinced. They point out that city academies still get some of the worst results in the country. Five of the 11 that announced GCSE results last year had not improved at all. Some have been criticised by the schools-inspection body, Ofsted, and one was placed in “special measures” to improve teaching standards. City academies spend 50% more per pupil than other new schools, the all-party committee on education of the House of Commons found last year. It recommended that funding for the £5 billion programme be withheld until the schools were shown to be cost-effective.

It is not just the schools' academic performance that raises eyebrows. A lot of the money has gone on knocking down scruffy old facilities and replacing them with new, visionary school buildings, ostensibly to raise pupils' aspirations. Some have proved disastrous rather than inspirational. The Bexley Business Academy, in Kent, had open-plan classrooms in which teachers struggled with noise levels; now walls are being built. In Brent, north-west of the centre of London, another academy is having to alter its vast, glass-panelled atrium. The Unity City Academy in Middlesbrough, in the Tees valley, was designed to look like a Tuscan village; Ofsted concluded it was not entirely fit for purpose. Sir Cyril Taylor, the chairman of the SSAT, promises an end to “glass palaces”. New buildings will be made of brick.

The controversy over city academies matters more than their numbers and budget suggest. They are, in a sense, the model for the sponsored, semi-autonomous “trust” schools that are at the heart of the prime minister's broader proposals to reform education, though trust-school sponsors would not be required to put up cash. Revelations that rich businessmen may have been allowed to think they would receive honours if they paid for an academy (which Mr Smith, for his part, denies) was bound to make headlines, especially given the bigger problems with murky political-party finances. But the bitterness of the row stems from a deep-seated opposition among state-school teachers and Labour Party left-wingers to Mr Blair's reforms.

Barry Sheerman, chairman of the education select committee, thinks the government should press on with the academies scheme, if rather more cautiously than at present. Yet further revelations could affect the education bill by strengthening its critics. Lord Levy, president of the SSAT and chief fundraiser for the Labour Party, is expected to be questioned by both police and two all-party select committees in the House of Commons. Scotland Yard has not ruled out interviewing the former schools minister, David Miliband, and possibly even Mr Blair himself.

Some speculate that, to save a policy in which so much has been invested, the government will turn away from wealthy individuals and reach out more to organisations such as churches, universities and further-education colleges instead. As they do, future academies might be rolled quietly into trust schools. Perhaps New Labour will learn that sponsors, like school buildings, are safest when most solid.

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Hyperactive children

Desperate parents,dangerous drugs

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Parents of hyperactive children face a dreadful dilemma

LIFE has just become even harder for parents of children with attention-deficit hyperactivity disorder (ADHD), a complaint that is said to account for many children's irritable unruliness and inability to concentrate. Many have had their doubts about the general wisdom of putting young children on drugs to help them focus. Now, it seems, there are specific side-effects that they should worry about.

Two committees of the body that regulates drugs in America, the Food and Drugs Administration (FDA), have recently reported adverse reactions to medicines that are often used to control ADHD. The most common of these drugs is Ritalin, an amphetamine-like stimulant (which, curiously, calms hyperactive people), but two others are also widely prescribed. They sometimes have unscripted side-effects.

Up to 5% of children may suffer hallucinations from the drugs, one committee warned. One child reported insects crawling under her skin, while another was surrounded by imaginary cockroaches. A second FDA committee looked at 25 reports of sudden death from heart problems and recommended that the drugs carry a black box warning about heart risk. The FDA is considering what other warnings should accompany the sale of such drugs.

Britain's Medicines and Healthcare Products Regulatory Agency (MHRA) is now reviewing the safety of drugs prescribed in England and Wales, in part because of the FDA reports. One of the three drugs used in Britain, Straterra, already carries a warning that it may provoke suicidal thoughts.

ADHD is a hard condition to diagnose. There is no medical test for it. A list of symptoms—including inattention, impulsivity and “overactivity”—is used to define the condition. In Britain, a specialist must diagnose the condition and the child must show that he is unable to function properly in two different settings.

Yet more and more children in developed countries are being diagnosed as having ADHD, and more are taking drugs for it. Rates are highest in the United States, where doctors themselves seem hyperactive with their prescription pads. Some 2.5m children and 1.5m adults there are on drugs for the condition, compared with 750,000 in 1987. Those figures include over 9% of 12-year-old boys, according to FDA data, and a staggering 17% of all white boys in the state of Virginia. In other rich countries, between 1% and 5% of the population is reckoned to suffer from ADHD.

In Britain, too, the number of those who take drugs for ADHD is going up. The National Institute for Clinical Excellence (NICE), which decides what drugs are used in England and Wales, said last month that 418,300 such prescriptions had been issued in 2004, most of them apparently to

children under 16 years old. The figure had almost doubled since 1998. Yet the chances of being prescribed drugs for ADHD differ widely from place to place, says Eric Taylor, of the Institute of Psychiatry. QIS Scotland, the health watchdog north of the Tweed, has launched an inquiry into the varying rates of Ritalin prescription.

Some psychiatrists argue that ADHD does not exist. They claim that drug companies and even doctors are pathologising normally-naughty childhood behaviour in order to create a market for drugs or to deal painlessly with a potentially time-consuming condition. The main ADHD charity in Britain, ADDISS, and the leading one in America, CHADD, have both received money from drug companies.

This may seem fanciful. But taking drugs is not always the route to success. Short-term studies find that children do concentrate better if they take drugs to calm them. Yet there is no convincing evidence that they have better grades as they leave secondary school than ADHD children who do not take drugs.

Many parents argue that medicine helps their child to function at school and enjoy a more normal life. Others dislike the weight-loss and insomnia that are commonly associated with the drugs, and would prefer to find a way to manage their child's behaviour or control his diet. But mental-health services for children are overstretched. Peter Hill, a consultant child psychiatrist, says that some patients wait 18 months for therapeutic help despite studies in America which show that behavioural therapy can work, on its own or combined with low doses of drugs.

NICE has only just agreed to compare the benefits of behavioural therapy with the effects of drugs. The report is expected in 2008. Until then children have little choice but to keep popping those pills.

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Company-law reform

Managing the playhouse

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A proposed new bill would invite judges into the boardroom

LORD ELDON, Lord Chancellor off and on from 1801 to 1827, is one of history's more unfortunate figures, remembered today (if at all) as an indecisive buffoon lampooned in Charles Dickens's "Bleak House" for never reaching a judgment. Yet his prudence laid the groundwork for almost two centuries of company law when he ruled in 1812 that courts should not be required to manage "every playhouse and brewhouse in the kingdom".

Behind Lord Eldon's words is a neat principle, usually known in America as the business-judgment rule. This holds that so long as the directors of a company act in good faith then their decisions (even the bad ones) will not be revisited by courts with the benefit of hindsight. Directors who are dishonest get judged in court and those that are just bad are judged in the market place. Now a proposed revision of England's company law threatens to change this arrangement.

The Company Law Reform bill, which has its last hearing in the House of Lords on April 25th, proposes to charge directors with more than safeguarding the financial interests of the companies they serve. They will also have to keep in mind their employees, customers and suppliers, as well as nurture communities and the environment. And the bill makes it easier for shareholders to sue wayward directors.

Critics, generally from business, warn that together these revisions threaten to release a torrent of litigation as suppliers, customers, environmentalists and others ask the courts to reverse company decisions. The mere threat of such suits may gum up board meetings as directors pay more attention to protecting themselves from legal action and less to doing what they get paid to do—taking risky decisions that may sometimes prove wrong.

Environmentalists and other non-profit groups, meanwhile, argue that the bill doesn't go far enough. An early-day motion before the House of Commons signed by 216 MPs calls for a tougher law to compel directors to "identify, consider, act and report on" any negative social and environmental impacts of their companies.

But not everything in the bill is contentious. The first big revision of English company law in more than 20 years, it introduces much-needed reforms, such as cutting the bureaucracy and cost involved in setting up and running a company. By explicitly allowing shareholders to sue rogue directors on behalf of the company, it clarifies a right that the courts already recognise. But the extension of directors' duties seems guaranteed to confuse, especially as some of them conflict.

The proposed duties are based on the notion that successful companies are also good corporate citizens, managed on behalf of "enlightened shareholders". Under this doctrine there is a neat intersection between the desire of shareholders for a better world and their interest in corporate success, and reward flows to those companies that are most successful at balancing the needs of

different stakeholders. But the approach bears little relation to reality.

Take tobacco and liquor companies. They supply products that, while giving pleasure, may harm their customers and others. Airlines provide convenient transport but also release greenhouse gases. Under the new law shareholders could potentially sue directors of these companies for disregarding their duty to protect the environment and the community. “You'll have the teetotallers taking over the brewery,” warns Dan Prentice, a law professor at Oxford's Pembroke College.

The greater worry is that, in trying to legislate good behaviour, the bill may make business decisions subject to subsequent review in court, says Adrian Levy, a partner at Clifford Chance, a law firm. Directors will be less happy to sanction a takeover or restructuring knowing that they could suffer personal liability for honest business decisions. In effect directors may end up being held liable for decisions simply because they are wrong, rather than because they acted in bad faith.

If the bill passes, many think judges will continue to leave business decisions to businessmen. Judges “are no good at it and don't want to take it on,” says Paul Davies, of the London School of Economics. Perhaps. But mounting red tape is already deterring qualified people from accepting board appointments. If they now face the risk of being taken to the cleaners for business decisions made in good faith, even fewer are likely to step forward.

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Bagehot

No more room for error

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Tony Blair is confident the NHS will pull through its latest crisis. Overly so

AFTER all the “NHS in crisis” headlines, the image of Tony Blair perspiring heavily as he delivered a second major speech in a week defending his health reforms was irresistible. Yet far from being worth a thousand words, the pictures were seriously misleading. Under baking television lights, the prime ministerial pores have a well-established tendency to open up. And, odd though it may seem since the recent news of spiralling hospital deficits and sacked nurses has been grim, Mr Blair is in fact serenely optimistic that his health policies are about to come good.

It is an optimism that is in marked contrast with his growing despondency about the prospects for his plans for secondary schools. Much of his party remains viscerally opposed to them and they are now further tarnished by the row over the honours allegedly promised to wealthy individuals in exchange for coming up with the cash to sponsor city academies. Even if his education bill survives the mauling that Labour MPs plan to give it, the trust schools that the reforms are meant to establish may suffer from the fallout.

From Mr Blair's point of view, what makes health a more promising bit of his legacy is that he reckons he has not only hit on the right model to reform the NHS but won the argument for it too. He also thinks there is some understanding that the NHS is going through temporary pain on the way to big gains in efficiency and quality of care. As he said in his speech: “We have now reached crunch point where the process of transition from one system to another is taking place.”

Mr Blair listed four “interlocking changes” that he believes will transform the “monolithic” health service into one that is devolved and decentralised, with “far greater power in the hands of the patient”. The first is practice-based commissioning, which gives incentives to general practitioners to transfer to hospitals only those patients who cannot be looked after more cheaply and better elsewhere. The second is a system that pays hospitals by results, based on a single tariff. The third change is to give patients the choice of who provides their treatment. The last is competition from new independent treatment centres for both elective surgery and diagnostics.

There are Labour diehards who accuse Mr Blair of privatising the NHS, while some on the right think he is merely tinkering with a doomed system. But Mr Blair is justified in claiming a broad consensus in favour of his reforms that includes independent think-tanks, most newspapers and probably a majority of MPs in both of the big parties. Mr Blair is also right to argue that change of this magnitude is necessarily disruptive and that political nerves have to hold while it is under way. But in almost every other respect, he is far too sanguine. The chances of failure are quite high, and for that the prime minister himself deserves much of the blame.

Mr Blair's attempts to construct a coherent narrative out of the health policies pursued by Labour since 1997 are specious and he surely knows it. He was at it again this week. But by appointing the Old Labour relic Frank Dobson as his first health secretary, and allowing him to scrap the internal market and GP fundholding set up by the Tories (now effectively re-established by Labour), Mr Blair set back the NHS by several years.

The consequences of not building on Tory reforms may, in fact, have been even more dire. When, in January 2000, Mr Blair was panicked into promising to raise health spending to the European average of 8% of GDP, the government still had no idea how the NHS should be structured to ensure that the huge sums of money it was preparing to throw at it would not be wasted. Mr Blair and Gordon Brown repeatedly warned that money would only follow reform, but just the opposite happened.

This week, Mr Blair tried to make it sound as if the huge pay rises doled out over the past few years to everyone who works for the NHS—the most egregious of which are the gold-plated GP contracts—was part of a carefully calibrated plan to build capacity while moving to new and self-sustaining structures. But Sir Derek Wanless, appointed by Mr Brown to provide the justification for nearly doubling spending in the seven years to 2007-08, gave the game away in a devastating and almost unreported interview a couple of weeks ago. The cost of salaries, Sir Derek said, had so far outstripped his projections that many of the assumptions in his report about what greater investment might achieve had been undermined.

Waiting for a miracle

The government's overspending on wages raises uncomfortable questions about whether the NHS and the Department of Health have the capability and expertise to design the patient-driven, demand-responsive systems that are now envisaged. Their former boss, Sir Nigel Crisp, has been booted into early retirement, but is there any guarantee that his replacement will do better? And even if the basic design is broadly correct, much of the devil will be in the detail. Will the quality of management information be adequate? Will the massive Connecting for Health IT programme deliver? Do hospitals and primary-care trusts have the kind of managers who can react to new and very different signals from the ones they are used to?

If the answer to any of those questions is negative, the prospects for the NHS after 2007-08, when the huge annual spending increases start to slow down, are bleak. Reform, a think-tank, estimates that, without what it calls a “productivity miracle”, the NHS could be facing a deficit of £7 billion ($12 billion) in 2010.

A streamlined and responsive NHS that efficiently allocates the generous resources given to it by the taxpayer could still emerge over the next few years. But the story of missed opportunities is lamentable and the degree of execution risk formidable. If that doesn't make Mr Blair sweat, it should.

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Among the audience

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The era of mass media is giving way to one of personal and participatory media, says Andreas Kluth. That will profoundly change both the media industry and society as a whole

THE next big thing in 1448 was a technology called “movable type”, invented for commercial use by Johannes Gutenberg, a goldsmith from Mainz (although the Chinese had thought of it first). The clever idea was to cast individual letters (type) and then compose (move) these to make up printable pages. This promised to disrupt the mainstream media of the day—the work of monks who were manually transcribing texts or carving entire pages into wood blocks for printing. By 1455 Mr Gutenberg, having lined up venture capital from a rich compatriot, Johannes Fust, was churning out bibles and soon also papal indulgences (slips of paper that rich people bought to reduce their time in purgatory). The start-up had momentum, but its costs ran out of control and Mr Gutenberg defaulted. Mr Fust foreclosed, and a little bubble popped.

Even so, within decades movable type spread across Europe, turbo-charging an information age called the Renaissance. Martin Luther, irked by those indulgences, used printing presses to produce bibles and other texts in German. Others followed suit, and vernaculars rose as Latin declined, preparing Europe for nation-states. Religious and aristocratic elites first tried to stop, then control, then co-opt the new medium. In the centuries that followed, social and legal systems adjusted (with copyright laws, for instance) and books, newspapers and magazines began to circulate widely. The age of mass media had arrived. Two more technological breakthroughs—radio and television—brought it to its zenith, which it probably reached around 1958, when most adult Americans simultaneously turned on their television sets to watch “I Love Lucy”.

Second incarnation

In 2001, five-and-a-half centuries after Mr Gutenberg's first bible, “Movable Type” was invented again. Ben and Mena Trott, high-school sweethearts who became husband and wife, had been laid off during the dotcom bust and found themselves in San Francisco with ample spare time. Ms Trott started blogging—ie, posting to her online journal, Dollarshort—about “stupid little anecdotes from my childhood”. For reasons that elude her, Dollarshort became very popular, and the Trotts decided to build a better “blogging tool”, which they called Movable Type. “Likening it to the printing press seemed like a natural thing because it was clearly revolutionary; it was not meant to be arrogant or grandiose,” says Ms Trott to the approving nod of Mr Trott, who is extremely shy and rarely talks. Movable Type is now the software of choice for celebrity bloggers.

These two incarnations of movable type make convenient (and very approximate) historical book-ends. They bracket the era of mass media that is familiar to everybody today. The second Movable Type, however, also marks the beginning of a very gradual transition to a new era, which might be called the age of personal or participatory media. This culture is already familiar to teenagers and twenty-somethings, especially in rich countries. Most older people, if they are aware of the transition at all, find it puzzling.

Calling it the “internet era” is not helpful. By way of infrastructure, full-scale participatory media presume not so much the availability of the (decades-old) internet as of widespread, “always-on”, broadband access to it. So far, this exists only in South Korea, Hong Kong and Japan, whereas America and other large media markets are several years behind. Indeed, even today's broadband infrastructure was built for the previous era, not the coming one. Almost everywhere, download speeds (from the internet to the user) are many times faster than upload speeds (from user to network). This is because the corporate giants that built these pipes assumed that the internet would simply be another distribution pipe for themselves or their partners in the media industry. Even today, they can barely conceive of a scenario in which users might put as much into the network as they take out.

The age of participation

Exactly this, however, is starting to happen. Last November, the Pew Internet & American Life Project found that 57% of American teenagers create content for the internet—from text to pictures, music and video. In this new-media culture, says Paul Saffo, a director at the Institute for the Future in California, people no longer passively “consume” media (and thus advertising, its

main revenue source) but actively participate in them, which usually means creating content, in whatever form and on whatever scale. This does not have to mean that “people write their own newspaper”, says Jeremy Zawodny, a prominent blogger and software engineer at Yahoo!, an internet portal. “It could be as simple as rating the restaurants they went to or the movie they saw,” or as sophisticated as shooting a home video.

This has profound implications for traditional business models in the media industry, which are based on aggregating large passive audiences and holding them captive during advertising interruptions. In the new-media era, audiences will occasionally be large, but often small, and usually tiny. Instead of a few large capital-rich media giants competing with one another for these audiences, it will be small firms and individuals competing or, more often, collaborating. Some will be making money from the content they create; others will not and will not mind, because they have other motives. “People creating stuff to build their own reputations” are at one end of this spectrum, says Philip Evans at Boston Consulting Group, and one-man superbrands such as Steven Spielberg at the other.

As with the media revolution of 1448, the wider implications for society will become visible gradually over a period of decades. With participatory media, the boundaries between audiences and creators become blurred and often invisible. In the words of David Sifry, the founder of Technorati, a search engine for blogs, one-to-many “lectures” (ie, from media companies to their audiences) are transformed into “conversations” among “the people formerly known as the audience”. This changes the tone of public discussions. The mainstream media, says David Weinberger, a blogger, author and fellow at Harvard University's Berkman Centre, “don't get how subversive it is to take institutions and turn them into conversations”. That is because institutions are closed, assume a hierarchy and have trouble admitting fallibility, he says, whereas conversations are open-ended, assume equality and eagerly concede fallibility.

Today's media revolution, like others before it, is announcing itself with a new and strange vocabulary. In the early 20th century, Charles Prestwich Scott, the editor, publisher and owner of the *Manchester Guardian* (and thus part of his era's mainstream media), was aghast at the word “television”, which to him was “half Greek, half Latin: no good can come of it.” Mr Scott's equivalents today confront even stranger neologisms. Merriam-Webster, a publisher of dictionaries, had “blog” as its word of the year in 2004, and the New Oxford American Dictionary picked “podcast” in 2005. “Wikis”, “vlogs”, “metaverses” and “folksonomies” (all to be explained later in this survey) may be next.

Word count

“These words! The inability of the English language to express these new things is distressing,” says Barry Diller, 64, who fits the description “media mogul”. Over the decades, Mr Diller has run two big Hollywood film studios and launched America's fourth broadcast-television network, FOX Broadcasting. More recently, he has made a valiant effort to get his mind around the internet, with mixed results, and is now the boss of IAC/InterActiveCorp, a conglomerate with about 60 online brands. Mr Diller concedes that “all of the distribution methods get thrown up in the air, and how they land is, well, still up in the air.” Yet Mr Diller is confident that participation can never be a proper basis for the media industry. “Self-publishing by someone of average talent is not very interesting,” he says. “Talent is the new limited resource.”

“What an ignoramus!” says Jerry Michalski, with some exasperation. He advises companies on the uses of new media tools. “Look around and there's tons of great stuff from rank amateurs,” he says. “Diller is assuming that there's a finite amount of talent and that he can corner it. He's completely wrong.” Not everything in the “blogosphere” is poetry, not every audio “podcast” is a symphony, not every video “vlog” would do well at Sundance, and not every entry on Wikipedia,

the free and collaborative online encyclopedia, is 100% correct, concedes Mr Michalski. But exactly the same could be said about newspapers, radio, television and the Encyclopaedia Britannica.

What is new is that young people today, and most people in future, will be happy to decide for themselves what is credible or worthwhile and what is not. They will have plenty of help. Sometimes they will rely on human editors of their choosing; at other times they will rely on collective intelligence in the form of new filtering and collaboration technologies that are now being developed. “The old media model was: there is one source of truth. The new media model is: there are multiple sources of truth, and we will sort it out,” says Joe Kraus, the founder of JotSpot, which makes software for wikis.

The obvious benefit of this media revolution will be what Mr Saffo of the Institute for the Future calls a “Cambrian explosion” of creativity: a flowering of expressive diversity on the scale of the eponymous proliferation of biological species 530m years ago. “We are entering an age of cultural richness and abundant choice that we've never seen before in history. Peer production is the most powerful industrial force of our time,” says Chris Anderson, editor of *Wired* magazine and author of a forthcoming book called “The Long Tail”, about which more later. (Mr Anderson used to work for *The Economist*.)

At the same time, adds Mr Saffo, “revolutions tend to suck for ordinary people.” Indeed, many people in the traditional media are pessimistic about the rise of a participatory culture, either because they believe it threatens the business model that they have grown used to, or because they feel it threatens public discourse, civility and even democracy.

This survey will examine the main kinds of new media and their likely long-term effects both on media companies and on society at large. In so doing, it will be careful to heed a warning from Harvard's Mr Weinberger: “The mainstream media are in a good position to get things wrong.” The observer, after all, is part of the observation—a product of institutional media values even if he tries to apply the new rules of conversation. This points to the very heart of the coming era of participatory media. It must be understood, says Mr Weinberger, “not as a publishing phenomenon but a social phenomenon”. This is illustrated perfectly by blogging, the subject of the next article.

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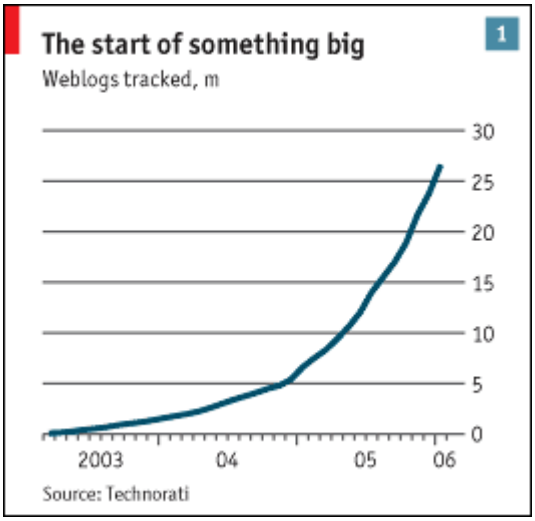
It's the links, stupid

Apr 20th 2006
From The Economist print edition

Blogging is just another word for having conversations



"IF YOU want to have a fun debate, ask bloggers what a blog is," says Jeremy Zawodny at Yahoo! Only a few years ago, that debate would have been short. So few people blogged that most of them knew one another and could probably agree on a definition. Today a new blog is created every second of every day, according to Technorati, a search engine for blogs, and the "blogosphere" is doubling in size every five months (see chart 1). From teenagers to corporate executives, the new bloggers all have reasons of their own for engaging in this new pursuit.

What, then, is a blog? A "personal online journal" is the definition that most newspapers, including *The Economist*, offer when they need to be brief. That analogy is not wrong, but nor is it entirely right (conventional journals usually come in chronological order, whereas blogs are displayed in reverse chronological order, with the most recent entry on top). More importantly, this definition misses the main point about blogs. Traditionally, journals were private or even secret affairs, and were never linked to other journals. Peeking into the diary of one's big sister typically led to a skirmish. Blogs, by contrast, are social by nature, whether they are open to the public as a whole or only to a small select group.

The word "blog" appears to date back to 1997, when one of the few practitioners at the time, Jorn Barger, called his site a "weblog". In 1999, another user, Peter Merholz, playfully broke the word into "we blog", and somehow the new term—blog—stuck as both a verb and a noun. Technically, it means a web page to which its owner regularly adds new entries, or "posts", which tend to be (but need not be) short and often contain hyperlinks to other blogs or websites. Besides text and hypertext, posts can also contain pictures ("photoblogs") and video ("vlogs"). Each post is stored on its own distinct archive page, the so-called "permalink", where it can always be found. On average, Technorati tracks some 50,000 new posts an hour.

Among the other technical features of blogs, two highlight the quintessentially social nature of blogging. The first is a "blogroll", along the side of the blog page, which is a list of links to other blogs that the author recommends (not to be confused with the hyperlinks inside the posts). In practice, the blogroll is an attempt by the author to place his blog in a specific genre or group, and a reciprocal effort by a posse of bloggers to raise each other's visibility on the internet (because the number of incoming links pushes a blog higher in search-engine results). The other feature is "trackback", which notifies ("pings") a blog about each new incoming link from the outside—a sort of gossip-meter, in short.

Blogging is also about style. Dave Winer, a software engineer who pioneered several blogging

technologies, and who keeps what by his own estimate is the longest-running blog of all (dating back to 1997), has argued that the essence of blogginess is “the unedited voice of a single person”, preferably an amateur. Blogs, in other words, usually have a raw, unpolished authenticity and individuality. This definition would exclude quite a few of the blogs that firms, public-relations people or newspapers set up nowadays. If an editor vets, softens or otherwise messes about with the writing, Mr Winer would argue, it is no longer a blog.

This explains the initial appeal of blogging as an outlet for pure self-expression. As Glenn Reynolds of Instapundit, a well-known blog on American politics, put it when asked why he blogs: “It beats yelling at the television.” But venting an opinion is usually only the start. “At first, I saw it as about publishing; now I see it more as a revolutionary way to communicate,” says Mena Trott. The company she runs with her husband Ben, Six Apart, illustrates this with its three main products. Their flagship, Movable Type, with its obvious publishing connotations, is a popular software service for heavy-duty or celebrity bloggers, including Mr Reynolds. So is TypePad, a similar service with web-hosting thrown in. Blogs powered by these two products have an average of 600 readers, says Ms Trott, although a few are read by more people than are some newspapers.

But Six Apart's third product, LiveJournal, is a very different kind of blogging tool. Some 60% of LiveJournal users are under 21 and female, says Ms Trott. Many of the posts are about who snogged whom last night and what happened next, why I'm sad, how adults don't get it, and so forth. Other posts ask things like, “Anybody want to catch King Kong at 8:00?” and have the replies in the comment pane below within minutes. That is because many adolescents consider e-mail passé, and instead are using either instant messaging (IM) or blogging for their communications, says Ms Trott. Like blogging, e-mail was supposed to be “asynchronous”, meaning that the people taking part do not have to be online simultaneously. But today's adolescents have never known e-mail without spam and see no point in long trails of “reply” and “cc” messages piling up in their in-boxes. As for synchronous communication, why adults would send e-mails back and forth instead of “IM-ing” is beyond them.

The Dunbar number

For these LiveJournal blogs, the average number of readers is seven, says Ms Trott. Such small audiences are common in participatory media. Indeed, they may conform to the biological norm, whereas mass-media audiences may have been an aberration. Robin Dunbar, an anthropologist at the University of Liverpool, has studied primates and discovered a surprisingly stable ratio between the relative size of the neocortex (thought to be responsible for the evolution of intelligence) and the size of groups formed by particular species. For humans, Mr Dunbar calculated, the upper limit is about 150. Many clans, tribes, fan clubs, start-ups and other groupings remain well below this limit, as do most blog networks.

The LiveJournal groups of readers are typical of the new-media era in another way. The bloggers (ie, creators) are one another's audience, so that distinctions between the two disappear. Creators and audiences congregate ad hoc in meandering conversations, a common space of shared imagination and interests. MySpace.com, a social-networking and blogging service that last year was bought by News Corporation, Rupert Murdoch's media conglomerate, reflects this quality in its name.

Conversations have a life of their own. They tend to move in unexpected directions and fluctuate unpredictably in volume. It is these unplanned conversational surges that tend to bring the blogosphere to the attention of the older and wider (non-blogging) public and the mainstream media. Germany, for instance, has been a relatively late adopter of blogging—only 1% of blogs are in German, according to Technorati, compared with 41% in Japanese, 28% in English and 14% in Chinese.

But in January this year “the conversation” arrived in Germany with a vengeance. Jung von Matt, a German advertising firm, had come up with a campaign in the (old) media called “Du bist Deutschland” (“you are Germany”). The advertisements were intended “to fight grumpiness” about the country's sluggish economy, said Jean-Remy von Matt, the firm's Belgian boss.

But German bloggers found the idea kitschy, and subsequently dug up an obscure photograph from a Nazi convention in 1935 that showed Hitler's face next to the awkwardly similar slogan “Denn Du bist Deutschland” (“because you are Germany”). In the ensuing online conversation, Mr von Matt's campaign was ignominiously deflated. Outraged, he sent an internal e-mail to his colleagues in which he called blogs “the toilet walls of the internet” and wanted to know: “What on earth gives every computer-owner the right to express his opinion, unasked for?” When bloggers got hold of this e-mail, they answered his question with such clarity that Mr von Matt quickly and publicly apologised and retreated.

Inadvertently, Mr von Matt had put his finger on something big: that, at least in democratic societies, everybody does have the right to hold opinions, and that the urge to connect and converse with others is so basic that it might as well be added to life, liberty and the pursuit of happiness. “It's about democratisation, where people can participate by writing back,” says Sabeer Bhatia, who in March launched a company called BlogEverywhere.com that lets people attach blogs to any web page with a single click. “Just as everybody has an e-mail account today, everybody will have a blog in five years,” says Mr Bhatia, who helped to make e-mail ubiquitous by starting Hotmail, a web-based e-mail service now owned by Microsoft. This means, Mr Bhatia adds, that “journalism won't be a sermon any more, it will be a conversation.”

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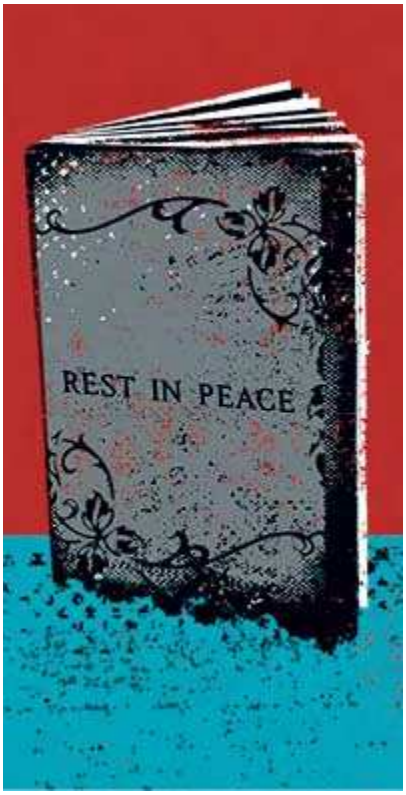
Compose yourself

Apr 20th 2006
From The Economist print edition

Journalism too is becoming interactive, and maybe better



"WE CHANGED South Korean politics and the media market, but I'm too shy to say that," says Oh Yeon Ho before he can catch his own irony. But Mr Oh, the founder and boss of *Ohmy News*, a sort of online newspaper, has earned the right to boast, because Ohmy is the world's most successful example to date of "citizen journalism" in action.

Ohmy's website currently gets an average of 700,000 visitors and 2m page views a day, which puts it in the same league as a large newspaper. But Ohmy has no reporters on its staff at all. Instead, it relies on amateurs—"citizens", as Mr Oh prefers to call them—to contribute the articles, which are then edited by Mr Oh, a former magazine journalist, and a few colleagues. Mr Oh likes to think of Ohmy as a "playground" for South Korean hobbyists, where "adults" set certain rules and thus give the site credibility. The articles tend to be good, because "in South Korea we have good people power," says Mr Oh. "They are highly educated and eager to change society." Ohmy also has built-in feedback and rating systems so that the best articles rise to the top.

One of Ohmy's biggest innovations is economic. The site has a "tip-jar" system that invites readers to reward good work with small donations. All they have to do is click a little tip-jar button to have their mobile-phone or credit-card account debited. One particularly good article produced the equivalent of $30,000 in just five days. Ohmy's own economics also appear to be working well. Even though Mr Oh originally intended the company to be not-for-profit—"my aim was not to earn money but to create a new kind of journalism," he says—he turned it into a for-profit firm in 2003. He will not divulge how much profit he makes, but the advertising and syndication revenues (from other internet sites that run Ohmy's articles) seem to keep him going nicely.

Ohmy's success has already had wide ramifications in South Korea's media industry. Although it has not killed off any South Korean newspapers or broadcasters, it has forced all of them to adjust by becoming more like Ohmy. Several newspaper sites, for instance, now have feedback and conversation panes at the bottom of online articles and are trying to interact more with readers. Mr Oh, who left his career in the mainstream media because he was sick of what he saw as their conservative bias, also reckons that Ohmy has helped to improve the balance. If the media scales used to be tilted 80% in favour of conservatives, he thinks, Ohmy has reduced that to 60%; he wants to make it 50%.

What works, and what doesn't

Does South Korea, a country of early adopters in many ways, foreshadow the future everywhere? “The reality is that you can't point to many successes; *Ohmy News* is the only one,” says Dan Gillmor, a journalist who quit his job at the *San Jose Mercury News*, a newspaper widely read in Silicon Valley, in order to found Grassroots Media, an experiment in American citizen journalism. After a year or so of looking in vain for a good business model, Mr Gillmor has put the idea on ice.

But others are much more optimistic. Last year Al Gore, a former American vice-president, and Joel Hyatt, his friend and business partner, set up Current TV, a cable-television channel that encourages its viewers to contribute their own video stories. And they do. “Viewer-created content”—or “VC2”,as Current TV calls it—now accounts for 30% of the channel's airtime, and rising. Mr Hyatt, the chief executive, thinks it will eventually be half or more. To help people get started, Current TV has extensive online tutorials on storytelling techniques, camera equipment and so forth. And to organise the content that comes in, its website allows users to vote on the quality of each video clip. It is, in many ways, a pure meritocracy.

When Current TV was launched, the traditional cable channels “didn't get it” and sneered, Mr Hyatt recalls with glee. “What people didn't understand is that there are tens of thousands of people out there who can create something great for a few minutes.” For instance, a story by an American traveller who found himself in the Gaza Strip during Israel's pull-out was probably the best piece of video reporting on the subject that ran on television at the time. During Hurricane Katrina, some residents of New Orleans made excellent contributions by taking cameras onto their home-made boats and making videos of their own neighbourhoods.

Yahoo! provides an even bigger example of the cheerful mixing of professional and amateur content (as opposed to Ohmy's insistence on the purely amateur). For instance, a lot of the articles, photos, audio and video on Yahoo! News come from corporate partners such as Associated Press or CNN. A tiny bit comes from Yahoo! itself (specifically, from Kevin Sites, a one-man camera team who travels to exotic and dangerous war zones around the world). But more and more content comes from citizens—Yahoo!'s users—says Scott Moore, who runs Yahoo!'s news and finance pages. Indeed, Yahoo! explicitly allows users not only to contribute content but also to take part in its filtering and placement, he says. These new collaborative processes even have a name—“folksonomies”—to distinguish them from the top-down “taxonomies” that human editors traditionally create.

For example, during the terrorist attacks on London's Underground last year, quite a few people in the wrecked trains took haunting photos with their mobile phones. They then wirelessly uploaded these to Flickr, a photo-sharing site owned by Yahoo! Other users then “tagged” these photos by attaching labels such as “London Underground” or “bombings” to them so that they could be easily found. The same or other users then spontaneously rated the pictures. This in turn brought the best pictures to the attention of Yahoo!'s human editors, who displayed them prominently alongside “professional” content across Yahoo!'s news sites. All of this happened within minutes.

The citizen journalism brought out by events such as the London bombings, Katrina, Asia's tsunami and other recent events has sent a new joke into the blogosphere: that Andy Warhol's proverbial “15 minutes of fame” have now become “15 megs” (megabytes) of fame for everybody on earth. That may be true. But the area of citizen journalism that is currently growing fastest, according to Mr Moore, is the least glamorous end: the so-called “hyper-local” coverage of, say, high-school sports or petty neighbourhood crime, which is usually too small even for local newspapers. This is one reason, says Mr Moore, why “in almost every market in the US we're already the number two provider of local news, after the leading local newspaper, and that's without even putting a lot of focus into it.”

For society as a whole, all this new talent—from bloggers, who are “journal-ists” in the classic sense, to citizen journalists—should amount to something overwhelmingly positive. “The more journalism the better; I don't care who does it,” says Dan Gillmor. That is not, however, how professional journalists, ostensibly speaking on behalf of the public, usually choose to see it. Their mood is gloomy.

Hard pressed

“Among our newspapers as they now stand, little more can be said in their favour than that they do not require batteries to operate, you can swat flies with them, and they can still be used to wrap fish.” Thus Joseph Epstein, a serial author, writing in the monthly magazine *Commentary*. Another author, Philip Meyer, makes his point in the title of his 2004 book, “The Vanishing Newspaper”. The last reader will recycle the last newspaper in April 2040, Mr Meyer estimates. If so, one of the most visible products of Gutenberg's movable type would expire eight years short of the printing press's 600th anniversary.

By common consent, the newspaper industry is in a perfect storm. In America, circulation has been gradually but steadily falling since 1990, according to *Editor & Publisher*, a trade journal. The trend in other countries is much the same. Most young people nowadays do not read a daily newspaper at all. To make matters worse (and to devalue the argument that society must preserve newspapers as “trusted” sources of news), the industry has been through a string of scandals, the most ignominious being the *New York Times*'s fiasco with Jayson Blair, one of its reporters who simply made up his stories. According to *The State of the News Media*, an annual American research project, the industry has laid off more than 3,500 newsroom professionals since 2000, about 7% of the total. In hard-hit Philadelphia, for instance, the number of reporters covering the metropolitan area is down to 220, half the 1980 figure.

Trends in advertising—and particularly classifieds, an inherently user-generated medium—are even bleaker. Whenever Craigslist.org, a do-it-yourself online bulletin board, enters a new city, local papers hear that proverbial sucking sound. EBay, the world's biggest auction site (which also owns a stake in Craigslist), already works like a global trading place. Last November, Google launched “Google Base”, a free service that allows users to upload anything—including classifieds—free of charge. These are consummate trading and advertising machines “for which journalism would be a ridiculous distraction”, says Mr Gillmor, who now works as an industry researcher. “That's hard to compete with if your main cost centre is journalism.”

Two bitter ironies serve to deepen the gloom. The first is that advertisers have been even slower to adjust than the newspapers themselves. After an admittedly delayed start, the papers are now getting better at helping their readers to move to their online offerings, so their customers as a whole are not actually defecting. But advertisers do not value the two media in the same way. Lauren Rich Fine, a financial analyst of newspapers, estimates that for every advertising dollar that a newspaper gets for a print reader, it receives only 20-30 cents for his online equivalent. Even though online advertising is growing by 30% or more a year, this is from a tiny base. Pip Coburn, an investment strategist, estimates that even newspapers such as the *New York Times*, which are widely read online, get only 5-10% of their revenues from the web.

The second irony—a common one for sunset industries—is that decline, financially speaking, is very pleasant. Printing presses, the main capital outlay for newspapers, last for decades and are depreciating peacefully with little need for new cash. As newspapers get rid of the more atavistic elements in their print editions—such as the pages of (inherently out-of-date) share prices—they also save on ink and paper. Thus, despite all the frightening circulation numbers, Goldman Sachs, an investment bank, estimates that the average profit margin for America's 12 biggest newspaper publishers in 2004 was 21%, more than double the average of the *Fortune* 500 companies. Some people are still making money, in other words, and are willing to invest. Last month McClatchy, a big American publisher, bought Knight Ridder, the country's second-biggest stable of newspapers, for $4.5 billion.

Old media fight back

But increasingly, newspaper barons, not content to preside over slow decline, want to embrace the revolution. One of them is Rupert Murdoch, chairman of News Corporation, one of the largest newspaper publishers in the English-speaking world. Last year he told the American Society of Newspaper Editors that “as an industry, many of us have been remarkably, unaccountably, complacent”. Young readers, Mr Murdoch said, “don't want to rely on a god-like figure from above to tell them what's important. And to carry the religion analogy a bit further, they certainly don't want news presented as gospel.” So what do newspapers need to do online to adjust? Their websites, Mr Murdoch said, “have to become the place for conversation. The digital native doesn't send a letter to the editor any more. She goes online and starts a blog. We need to be the destination for those bloggers.” Soon after this speech, Mr Murdoch bought MySpace, an online blogging and social-networking site wildly popular with young people.

Rhetorically, Mr Murdoch hit all the right notes. Implementing this soaring vision, however, is difficult in practice. Exactly how does an august publication turn itself into a “place for conversation”, especially given that all sorts of lively conversations are already in progress in the blogosphere? Last year, the *Los Angeles Times* gave it a go. Michael Kinsley, its opinions-page editor at the time (as well as a former co-host of CNN's “Crossfire” show and a founder of *Slate*, an online magazine) turned his page into a “wikitorial” in which readers could edit articles (more on wikis in the next article). This did not work at all. Vandals converged on the wiki and wrecked it, until the newspaper shut it down and parted with Mr Kinsley. The *Washington Post*, too, experimented with a blog open to outsiders, and also shut it down after a spate of vandalism.

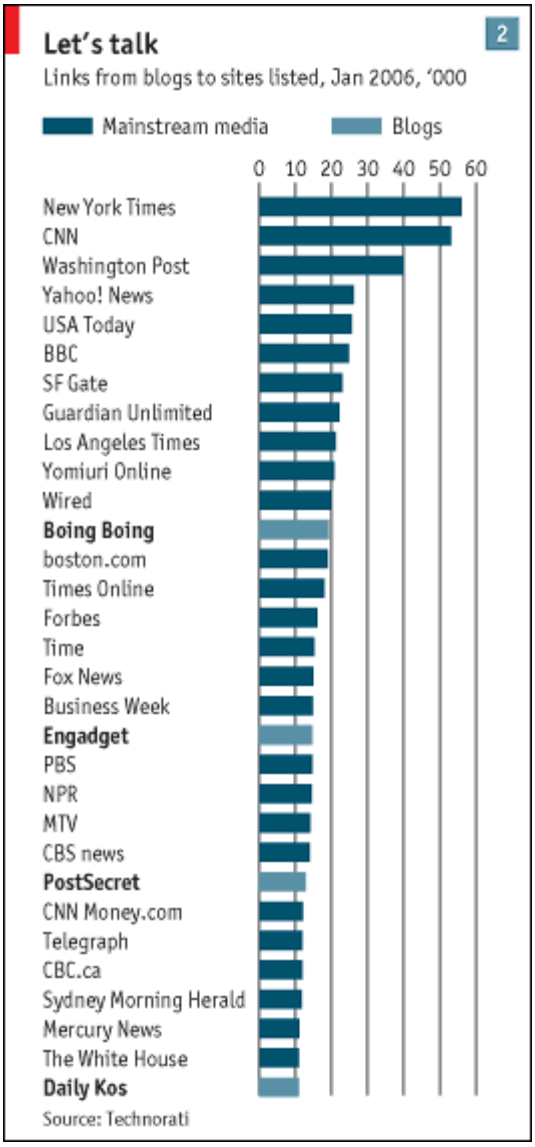
The worst conclusion that newspaper owners could draw from such setbacks is that interactivity does not work and should be avoided. “It's like saying, ‘I hear there are assholes in New York, so I'm not going there'; yes, there are assholes, but you should still go there because we can figure out who the assholes are,” says Jeff Jarvis, a former journalist and newspaper consultant who blogs at Buzzmachine.com. He suggests joining the online

conversation in ways that are appropriately circumspect.

The first step, says Mr Jarvis, is to tear down any walls around the website. Nowadays "it's not content until it's linked," he says, and bloggers will not link to articles that require logins and subscriptions to be viewed. This has immediately obvious effects (see chart 2). The sites that bloggers link to most are the online *New York Times*, CNN, the *Washington Post*, Yahoo! News, *USA Today* and the BBC. These are free or mostly free sites and thus, in effect, part of "the" conversation, because they are already part of a great many conversations.

By the same logic, news sites should avoid the still surprisingly common internet sin called "link-rot". This refers to websites that publish an article under one web address (or URL, for "uniform resource locator"), but then change the URL when archiving the article. "If you break your links, you break your inventory," says Jerry Michalski, the media consultant, "and nobody links to rotting links."

Free access and permanent links are two specific examples of a new "story-centric" approach that Jupiter Research, an internet consultancy, advises newspaper companies to adopt for their web editions. Instead of assuming that readers will start on the front page, editors should expect them to enter at any point, probably having started out from Google's search page or a blog or an e-mail from a friend with a link. This makes a big difference. It means that every single page needs navigation aids to help readers along in their journey. For publishers, says Jupiter, it requires "deconstructing their websites—treating individual stories (and not the website) as their most important product."



The next step is to allow—indeed, encourage—reader participation on individual pages. This could start with a simple star-rating system of each article. Deeper engagement would include comment panes at the bottom of stories (like those below blog posts), or blog discussions between the journalists and invited guests. As with some group blogs today, contributors could be required to log in, either under their real name or a pseudonym. This leaves reputation trails and discourages vandalism. "Just as more blogs will look like newspapers, more newspapers will have blog-like aspects," says Paul Saffo at the Institute for the Future.

Admittedly, this kind of advice can sound like woolly new-age claptrap to newspaper publishers. They want to know whether there will still be a long-term business model for things like investigative reporting and fact-checking. Ironically, they are finding support among their internet rivals, who tend to be idealists. Craig Newmark, of Craigslist, says that "journalism needs to become a community service rather than a profit centre," and is working on making this happen. As *The State of the News Media* puts it, "the worry is not the wondrous addition of citizen media, but the decline of full-time, professional monitoring of powerful institutions." That, after all, is what a free press in democracies is supposed to be for.

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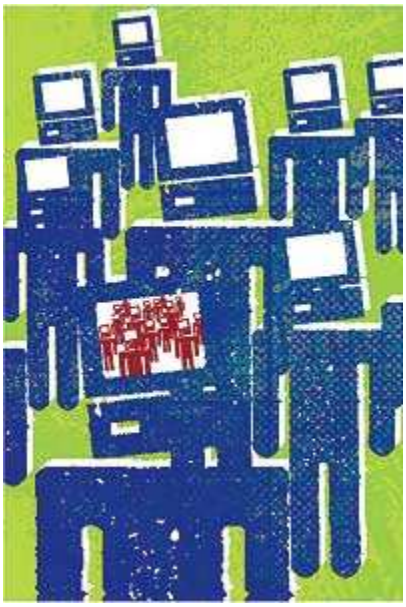
The wiki principle

Apr 20th 2006
From The Economist print edition

Are many minds better than a few?



WHEN people express scepticism about participatory media, they usually have people like Brian Chase in mind. Mr Chase is a 38-year-old from Nashville, Tennessee, who until recently worked in the middle-management layers of a courier firm called Rush Delivery and seemed destined to remain entirely unremarkable. For reasons known only to himself, however, Mr Chase last May decided to play a joke, "a joke that went horribly, horribly wrong", as he would later tell his local newspaper, the *Tennessean*.

His joke consisted of a hoax entry on Wikipedia.org, a free online encyclopedia that anybody—anybody at all—can edit, simply by clicking on a button that says "edit this page". Mr Chase posted a biographical article on John Seigenthaler, a distinguished journalist (and former editor of the *Tennessean*) who in 1961 did a stint as assistant to Robert Kennedy, America's attorney-general at the time. Mr Chase, however, fabricated an entirely different life for Mr Seigenthaler, one that had him living in the Soviet Union, founding a public-relations firm and, most perniciously, suggested that he was implicated in the assassinations of both John and Robert Kennedy.

Normally, such vandalism is corrected within minutes on Wikipedia because other people see it, remove it and improve the entry with their own genuine insight—that, in a nutshell, is the philosophy and power of collaborative intelligence. This particular item, however, fell through the cracks. For 132 days, the libellous lies went unnoticed and remained on the site. Eventually, some volunteer sleuths traced the vandalism to Mr Chase, who finally came clean last December and apologised profusely to an impressively gracious Mr Seigenthaler. With that, the episode became a scholarly footnote in media history.

A telling one, however. Reflecting on the incident in *USA Today*, Mr Seigenthaler succinctly summarised the promise and peril of the latest media revolution: "And so we live in a universe of new media with phenomenal opportunities for worldwide communications and research—but populated by volunteer vandals with poison-pen intellects."

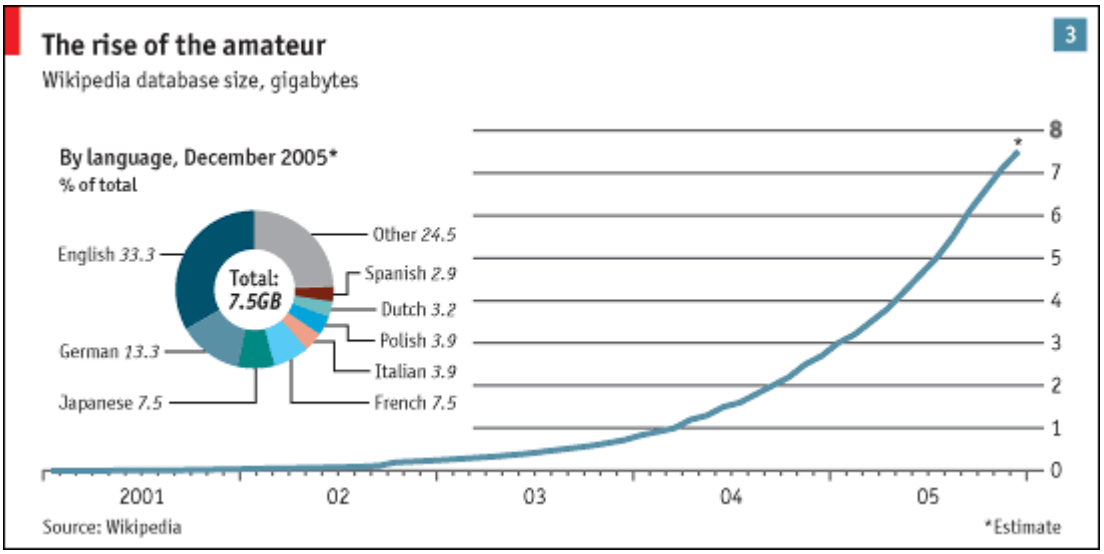
For the most part, it is much more worthwhile to dwell on the phenomenal opportunities than on the poison pens. Wikipedia's promise is nothing less than the liberation of human knowledge—both by incorporating all of it through the collaborative process, and by freely sharing it with everybody who has access to the internet. This is a radically popular idea. Wikipedia's English-language version doubled in size last year and now has over 1m articles. By this measure, it is almost 12 times larger than the print version of the Encyclopaedia Britannica. Taking in the other 200-odd languages in which it is published, Wikipedia has more than 3m articles. Over 100,000 people all over the world have contributed, with a total of almost 4m "edits" between them. Wikipedia

already has more “visitors” than the online *New York Times*, CNN and other mainstream sites. It has become a vital research tool for huge numbers of people. And Wikipedia is only five years old.

This success has made Wikipedia the most famous example of a wider wiki phenomenon. Wikis are web pages that allow anybody who is allowed to log into them to change them. In Wikipedia's case, that happens to be anybody at all. The word “wiki” comes from the Hawaiian word for “quick”, but also stands for “what I know is...”. Wikis are thus the purest form of participatory creativity and intellectual sharing, and represent “a socialisation of expertise”, as David Weinberger, who is currently writing a book on collaborative intelligence, puts it.

Among the new media, wikis are the perfect complement to blogs. Whereas blogs contain the unedited, opinionated voice of one person, wikis explicitly and literally allow groups of people to get on the proverbial “same page”. This is the main reason for the failure of a *Los Angeles Times* experiment with wikitorials, described in the previous article. Wikis are good at summarising debates, but they are ill-suited for biased opinion.

Wikipedia's numbers actually make it an anomaly among wikis. Joe Kraus, the co-founder of JotSpot, a provider of wiki software, reckons that most of the millions of wikis already in existence are designed for small, well-defined groups of people. Team members in a company, for instance, might use wikis to collaborate on presentations or project calendars. Wikis are communities, and “communities require trust,” says Mr Kraus. Trust comes most easily when the people involved know one another or are accountable for their contributions. Given that the optimal group size for humans may be less than 150 members (see the article on blogging earlier in this survey), most wikis might be expected to be small.



Darwin or intelligent design?

At first sight, Wikipedia seems too large for its contributors to be able to trust each other easily. How, then, does it work? A common assumption, expressed most cuttingly by Robert McHenry, a former editor-in-chief of the Encyclopaedia Britannica, is that Wikipedians trust in “some unspecified quasi-Darwinian” process, whereby accuracy “evolves” as more and more “eyeballs” examine an item. “Does someone actually believe this?”, wonders Mr McHenry. He obviously does not. To him, Wikipedia is a “faith-based encyclopedia”, based on “the moist and modish notion of community and some vague notions about information wanting to be free”.

In fact, it turns out that such quasi-Darwinian logic is “not the way we talk about ourselves within the community”, says Jimmy Wales, who started the (not-for-profit) Wikimedia Foundation that operates Wikipedia, as well as lesser-known sites such as Wiktionary, Wikinews and Wikibooks. Instead, says Mr Wales, the process “is much more traditional than people realise”. Fewer than 1% of all users do half the total edits. They add up to a few hundred committed volunteers like himself, says Mr Wales—“a real community of people who know each other” and value their reputations. Besides “democracy” on the site, he says, there is occasional “aristocracy” (when editors with superior reputations get more say than others) and even occasional “monarchy” (“that's my role”) in cases such as the Seigenthaler biography, when quick intervention is needed.

To put this process to the test, the journal *Nature* recently commissioned a study to compare the accuracy of a sample of articles drawn from Wikipedia and the Encyclopaedia Britannica respectively. Nature's experts found 162 errors in Wikipedia's articles and 123 errors in Britannica's. Jorge Cauz, Britannica's president, immediately claimed victory because Wikipedia had “a third more errors”.

We are all fallible

Privately, however, Britannica's editors were shocked to have to concede that their creation contained any errors at all. Total accuracy, after all, is the main selling point for the old media. So Dale Hoiberg, Britannica's current editor-in-chief, commissioned his own review of the study and found that “*Nature* did everything wrong that they could possibly have done wrong.” Last month *Nature* issued a rebuttal. But if it did get it wrong, it is not clear why it would have erred more for Britannica than for Wikipedia. Mr Hoiberg puts a brave face on it, claiming that “our model, although not perfect, is the best.”

For a lot of new-media watchers, the most interesting thing about the episode was something entirely different: that Britannica, somewhat representative of old media in general, instinctively regards Wikipedia as a threat, whereas Wikipedians are not the least bit tempted to reciprocate. “I'm a big fan of Britannica's work,” says Mr Wales, adding that he is not motivated by “disrupting” anybody, and is glad that Brockhaus, the biggest encyclopedia in Germany (where Wikipedia is very popular), appears to be doing better than ever. But why not have a free alternative as well? And why not test the limits of what social collaboration can do? Mr Wales is the first to admit that “there are some inherent limitations,” and says they are busy trying to discover what they are.

Contrast that with the joyful reaction of Wikipedia's detractors to Brian Chase, the dodgy biographer (whose article was literally one in a million). Somebody who reads Wikipedia is “rather in the position of a visitor to a public restroom,” says Mr McHenry, Britannica's former editor. “It may be obviously dirty, so that he knows to exercise great care, or it may seem fairly clean, so that he may be lulled into a false sense of security. What he certainly does not know is who has used the facilities before him.” One wonders whether people like Mr McHenry would prefer there to be no public lavatories at all.

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Heard on the street

Apr 20th 2006
From The Economist print edition

Podcasting will change radio, not kill it

BLOG and wiki were already dictionary words in 2004 when Adam Curry, a former show host on MTV, used his own celebrity and the underlying technologies of blogging to popularise yet another next big thing: "podcasting" (which provided him with a new nickname, "podfather").

The word itself is hip but not helpful. The "pod" comes from Apple's iPod, a fashionable portable music player—a stroke of marketing luck for Apple, which initially had nothing to do with podcasting. The "casting" comes from broadcasting, which means sending a radio signal to an entire population in a particular geographic area at a particular time. Confusingly, in some respects that is the opposite of podcasting. But none of this matters any more. As with blogs and wikis, people are discovering podcasting as something genuinely new.

It works as follows. A podcaster records something—anything from music to philosophical ramblings, professional news or snorting noises—into a computer with the aid of a microphone, then posts this audio file onto the internet. There, people can listen to it and, more importantly, subscribe to a "feed" from the same podcaster, so that all new audio files from that source are automatically pulled down as soon as they are published. Whenever listeners dock their iPods or other music players for charging, the feeds that have newly arrived on the computers are transferred to the portable devices. People can then listen in their car, while jogging, or wherever and whenever they please.

It is not quite true, therefore, that podcasting is to audio as blogging is to text. Podcasting is about "time-shifting" (listening offline to something at a time of one's own choosing, as opposed to a broadcaster's), whereas reading blogs requires a live internet connection and a screen. More subtly, podcasts are different from blogs and wikis in that they cannot link directly to other podcasts. This makes podcasting a less social, and probably less revolutionary, medium.

Nonetheless, its rise has been nothing short of astonishing. Mr Curry's own podcast, *The Daily Source Code*, has several million listeners. Apple's iTunes, the software application and online music store that makes iPods work, currently lists 20,000 free podcasts and is adding them at a fast clip, all before podcasting's second birthday. Podcasting is even expanding from audio to video, although this trend is as yet so new that several words ("vodcasting", "vidcasting" , "vlogging") are still vying for the honour.

For listeners, the appeal is threefold. First, they become their own programmers, mixing the music and talk feeds that they enjoy. This liberates commuters, say, from commercial radio stations that, in America especially, seem only ever to get dumber and duller. Second, podcasts liberate listeners from advertising, and thus put an end to the tedious and dangerous toggling between the

car radio's pre-set buttons at 100km an hour. (However, some podcasters are experimenting with putting advertisements into their podcasts.) Above all, the time-shifting that podcasts make possible liberates people from having to sit in their parked cars to hear the end of a good programme.

For creative types, professional or amateur, the appeal of podcasting is much the same as that of other participatory media: it dramatically lowers the costs of producing content. All they need is a microphone, a computer and an internet connection, and most people already have those.

Hammed radio

Does podcasting therefore spell the end of radio? “I don't really buy into that per se; what we're really seeing is a big mash-up of stuff,” says Mr Curry, the podfather. Podcasting, terrestrial radio and another newcomer, paid-for (ie, mostly advertising-free) satellite radio, are all carving out their niches in people's crowded media lives. The limiting factor of podcasting, says Mr Curry, is that it is “inherently asynchronous” (ie, not live). “If they find Osama bin Laden, don't go running to your iPod,” he adds. Breaking news, call-in shows (an old-fashioned form of participatory media) and other live programming will still work on terrestrial radio.

This might lull radio bosses into a false sense of security, however. “I'm not sure that the average consumer is going to want to hear, you know, Joe podcasting out of his garage,” says Mark Mays, the chief executive of Clear Channel Communications, America's largest radio broadcaster with 1,200 commercial stations. Mr Mays claims that when people buy an iPod they will reduce their radio listening for a few months, but then increase it again to educate themselves about new music. “And where else to go for music than their local radio station?” asks Mr Mays.

If they are young, they will go anywhere but to their local radio station, says David Goldberger, the music boss at Yahoo! “The odds that you and I like the same five songs in a row are very low,” he says. “If you hate Metallica, you're not going to sit through three minutes hoping that the fourth minute gets better.” To young people today, song sequences are simply “playlists”, which happen to be among the easiest things to share with friends online, so this is what Yahoo! concentrates on doing. It lets people listen to music (for a small monthly subscription or pay-by-download) and then rate the song. Yahoo! then uses its knowledge of the online communities formed by its users to recommend the right kinds of songs “by connecting you with other people who like the same music”, says Mr Goldberger.

The effects on radio, while not lethal, will therefore be large. Radio broadcasters understand that they need to make commercial radio less disagreeable to listen to, which above all means shorter advertising interruptions. This is why Clear Channel has introduced a campaign called “less is more”, in which it sells fewer minutes to advertisers in the hope that this will drive up ratings and prices.

Historically, radio has been good at adapting. When Franklin Roosevelt gave his “fireside chats”, radios were in the living room and families gathered round them during prime time. Then television came along, and radios migrated to the car for use during rush hours. Podcasting may herald yet another migration, to a place and context yet to be determined.

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Wonders of the metaverse

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From The Economist print edition

A fantasy world where people make their own films

“LET'S build a really cool swing and see if we can get somebody to sit on it,” says Philip Rosedale. A few clicks later, there is the swing, and quite an artful one. Onlookers have gathered to watch. One, named “mermaid”, declines to sit on the swing, but another, called “ninja”, hops on and rides for a bit. Then a dragon comes along that is so beautifully crafted that everybody stares.

Technically, all this is happening not in real life but in Second Life, a “metaverse” (for “metaphysical universe”) created by Linden Lab, a San Francisco internet company. Mr Rosedale, its founder, says that Second Life is “not a video game but a place where people make things.” This is hard to imagine until one sees it, but then instantly addictive. People who log on to Second Life create an “avatar” (ie, an online extension of themselves). As avatars, they mingle, go to parties, create what they wear and drive in, build the houses where they live, paint pictures and compose music.

Second Life is not as separate from real life as one might expect. Larry Lessig, a real-world author, recently gave a book talk in Second Life, and lots of avatars showed up. People own copyright in real life for the things they create in Second Life. Avatars trade their creations in “Linden dollars”, convertible into hard dollars on Linden's currency exchange, which has a monthly trading volume of $4m. One user, Anshe Chung, pays Linden Lab the equivalent of about $200,000 a year to buy land in Second Life. Ms Chung turns a profit by developing this land into residential communities (such as “Hangzhou”, “Gotland”, “Emerald Island” and so on) and charging avatars rent. “It's the purest way of profiting from creativity,” says Mr Rosedale.

A lot of the things created in Second Life are exported into real life, as fashion, songs and so on. One user, Natha Keir (whose avatar is called Kermitt Quirk) created an online multiplayer game called Tringo, which is a bit like bingo but more fun. Tringo started as a game within the game but has now taken on a life of its own outside Second Life.

Other avatars have created cameras and are filming things that happen in Second Life. In effect, some avatars become actors for other avatars who become directors. These new directors then post their films to websites in real life (“real” having become a slippery concept by now). “You can be the next Coppola here,” says Mr Rosedale, as he watches one such film, in which a cowboy is just sauntering into a saloon and gun-slinging appears imminent. “Second Life reduces the cost of filming a movie to zero.”

Second Life opened in 2003 and is now inhabited by about 100,000 people from around the world (still a small number compared with the video-game giants). Unlike earlier generations of video games, which appealed mainly to narrow demographic groups, Second Life is popular with women as well as with men, and with middle-aged people as well as teenagers. If there is a trend, Mr Rosedale says, it is perhaps that Second Life does best in places with bad weather, fast broadband connections and unexciting entertainment options. He considers British suburbs an excellent growth market.

In time, metaverses could disrupt the economics of mainstream film-making. Philip Evans at Boston Consulting Group estimates that Linden Lab has so far invested about $25m into the Second Life environment. But as “about 90% of the content is created by the players”, calculates Mr Evans, this works out at a total “investment” of perhaps $250m, which brings Second Life up to the budgets of Hollywood blockbusters. “The production values are amazing,” says Mr Evans. This potential economic disruption to Hollywood, he thinks, “could be the harbinger of something very much bigger.”

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The gazillion-dollar question

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So what is a media company?

FOR his first few decades in the media industry—at CBS, then Walt Disney, then Warner Brothers, where he was chairman and co-chief executive—Terry Semel felt pretty clear about what media companies were. He was running them, after all. Then, in 2001, he left Hollywood and went to Silicon Valley as the new boss of Yahoo!, the world's largest internet "portal" (gateway). A self-avowed technophobe who barely knew how to use e-mail, Mr Semel suddenly found himself in "meetings with a bunch of 23-year-olds". He already had the ambition to turn Yahoo! into the archetypal "21st-century media company", but suddenly he was no longer so clear on what that meant.

Mr Semel has spent the past five years educating himself, counselled by trusted advisers such as his daughters, aged 24, 19 and 13. The first does a lot on the internet, the second does everything on the internet, and the third "lives online" and has so many beeping devices that Mr Semel, who has a New York accent and the kind of humour that goes with it, occasionally wonders "whether she is trafficking". Between them, they have helped him to work a few things out.

The internet "is a much larger change than the coming of television" in the 20th century, says Mr Semel. In the past, "someone decided that the news goes on at 11 o'clock at night; people like my wife never even saw the news, because she never stayed up that late. We all grew up when somebody else was the programmer; now the user is the programmer." That is change number one. To Mr Semel it means that Yahoo! must do more than provide technology. "We decided to open Yahoo! up, so that anybody using [their personalised start page] MyYahoo! can instantly go wherever they want to go," even if that leads to the web pages of rivals. That credibility, he thinks, will keep users coming back for a "deeper engagement". As people spend more time on Yahoo!'s pages—news, blogs, e-mail, chat groups, photo and music sites and so on—whether as their final destination or as stops on a journey, Yahoo! can put more and better advertising in

front of them.

Change number two, says Mr Semel, is that—unlike in television, say—"you don't need hits". Many small audiences are as good for advertisers as few large audiences, and indeed may be better. This has huge implications for content, turning it into one long continuum—from professional to amateur, from blockbuster to subculture niche. Chris Anderson of *Wired* magazine calls this stretched statistical distribution "the long tail". In his forthcoming book of the same title, Mr Anderson argues that old-media economics, which are biased toward the hits at the "head" of this distribution, are being replaced by new-media economics, which allow creation and consumption along the entirety of a much longer content tail.

Yahoo!, says Mr Semel, will therefore be happy to mix professional content and user-generated content, no matter how small its potential audience, on its pages. The general direction, however, is towards ever more user-generated stuff. In March, Yahoo! said that it would limit its own production of content.

Where does all this lead? "It will look more and more like a stock exchange," says Mr Semel. An exchange, that is, for users who "offer" (create) and "bid" for (search, navigate, share, enjoy) content. And a stock exchange for advertisers, who bid against one another to have their sponsored links placed in front of these users.

Open outcry

To most old-media executives, the conversation turns baffling at this point. They find it much more reassuring to insist that, in one sense, media companies will probably never change. They are still, at heart, audience aggregators that make money by selling advertising to third parties who want to reach those audiences, or by charging the audiences directly through subscriptions, or a bit of both.

Upon closer examination, this is not so reassuring. Using this definition, the media industry now includes strange newcomers. Google, for instance, "happens to be a media company run by technology people", says Larry Page, its co-founder, because virtually all of Google's revenues come from advertising. In fact, Google is the most valuable media company in the world, with a market capitalisation about half as large again as that of Time Warner, the largest "traditional" media company. This is remarkable because Google, an internet search engine with lots of other free internet services, explicitly does not produce that which media companies have traditionally manufactured: content.

"We're engaged in a semantic exercise," says Jeff Bewkes, the number two at Time Warner. "Is Google a media company? It's a weird discussion, what is a media company." Ultimately, he thinks, "everyone is going to the same media place but they're coming through different doors to get there." This still begs the question: What does that place look like? And do all the doors provide equally good access?

"The history of the world would suggest that the newer companies that were designed for the medium will prevail, and will then combine," says Jonathan Miller, the boss of AOL, a rival to Yahoo!, partner in search technology to Google and itself part of Time Warner. That is because the newcomers are at ease in the long tail of content, whereas old-media firms tend to get stuck trying to generate hits.

Exchanges become necessary because people need help navigating around this huge continuum of content. In the present century, says Paul Saffo of the Institute for the Future, "you get large by allowing the many and small to gather on your lawn." This is the media equivalent of what eBay, a

Silicon Valley neighbour to Google and Yahoo!, has done for the trading of secondhand goods among individuals. It is what Wikipedia has achieved as an encyclopedia. It is also very similar to what, say, the New York Stock Exchange does.

Vinod Baya and John du Pre Gauntt at PricewaterhouseCoopers, a consultancy, argue exactly this in a report called “The Rise of Lifestyle Media”. Successful media companies, they write, will become “marketplaces that let consumers search, research, share and configure their media experiences.” To be good, these exchanges need to combine “a personalised media experience with a social context for participation.” Instead of “exclusive ownership of content or distribution assets” (the stuff of old media), the media marketplaces will compete in their “knowledge of consumer activity”, which they will use both to interact more intimately with consumers and to match them better to advertising that is unobtrusive and helpful (itself a novelty), and thus lucrative.

The analogy to marketplaces has another important implication: network effects. The value of networks (such as the telephone or postal systems) and exchanges (such as eBay or the New York Stock Exchange) increases dramatically as the number of participants rises. Once achieved, network effects also become barriers to entry by rivals. If they are looking for an exchange, for instance, both buyers and sellers will gravitate towards the market with the greatest liquidity in a given share or bond.

This is why a lot of new-media companies are now hurrying to create marketplaces with network effects before somebody else does. YouTube, a start-up launched about a year ago, lets people upload and share their own videos. It already transfers more data each day than the equivalent of an entire Blockbuster video-rental outlet. It goes without saying that Time Warner's AOL, Google, Yahoo!, Amazon and other internet companies are also working to exploit network effects.

This race to become the most liquid media marketplace has just started, and the winners are not yet obvious. But the giants, Yahoo! and Google, do have a head start. They already have network effects in their advertising, and emerging network effects in some types of media (text-based blogging, say) that can be transferred to other types (such as video). That is because the distinctions between different types of digital files are becoming increasingly unimportant (assuming a good broadband connection). To savvy teenagers, it's all just stuff passed around among friends.

A tale of two markets

As it happens, Yahoo! and Google have very different visions about what a media exchange should look like. This might be surprising, because on the surface the two companies are very similar. Their headquarters are in adjoining and equally drab suburbs; each was founded by two friends at Stanford University; and “both have assembled audiences of users the likes of which the world has never seen,” says Michael Moritz at Sequoia Capital, the lucky venture capitalist who early on invested in both of them.

But Jerry Yang and David Filo, Yahoo!'s founders, started their company as a hobby, says Mr Moritz. It was always meant to be a media company, and a rather relaxed, human one at that. Larry Page and Sergey Brin, by contrast, have always been “intellectually obsessed” with their mathematical algorithms, says Mr Moritz. This shows. Today, Yahoo! does interesting research into the sociological aspects of the internet, whereas Google hires the world's top computer geeks.

This is not unlike, say, the rivalry between the New York Stock Exchange (with its tradition of open-outcry floor traders) and the NASDAQ (where trading has always been done by computers). In news, for instance, Google displays stories selected by computer algorithms, whereas Yahoo!

uses human editors to select the line-up. Caterina Fake at Yahoo! (and the co-founder of Flickr) says that Google's people “solve problems by brute-force computation”, whereas Yahoo!'s approach is “about people, behaviours, sociology”. Speaking for Google, Tim Armstrong, its advertising boss in North America, counters that Yahoo!'s talk about “creating a community has some of that old-media tone about it; is the future for corporate-created communities or user-created communities? Google has a high trust level in users.”

It is a religious war, in short, but one where worshippers for once get the benefit. Yahoo! is working on the social “folksonomies” described earlier in this survey. Google is working on solving problems such as providing (without charge) the enormous online storage required for all this uploading of media files. It is also working on the economics to ensure that not only Google but its users too get some of the financial benefits of their creativity. Google Video, for instance, is a service (or rather, the rough draft of one) in which Google lets anybody upload video. The main innovation is that the creators can determine whether their video is free or has a price. If it is charged for, the creators get 70% of the purchase or rental money and Google keeps the rest.

Where does all this leave old-media companies? For a number of years, they might continue to do well without changing, because many innovations (like Gutenberg's movable type) take decades to become mainstream. A few of these companies stand a decent chance of turning themselves into a genre-specific brand (such as “family content” for Walt Disney). Others, such as Viacom, which recently split its distribution and content into separate companies, are preparing for a future as content producers at a specific point in the “tail”. Yet others, such as News Corporation and Time Warner, are staying vertically integrated for now, and trying to combine old-media empires with new-media marketplaces (MySpace and AOL, respectively). But this is risky, since “in an attempt to protect the one you could screw up the other,” as Mr Evans at Boston Consulting Group puts it.

For old-media moguls who have become new-media moguls, such as Yahoo!'s Mr Semel, all of this is tremendous fun to watch. “Until recently they were just being protective, keeping their arms around their copyright,” says Mr Semel about the old industry that he left behind. “The faster they start to pay attention to making stuff for people like Yahoo!, the better for them.” They've been warned.

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What sort of revolution?

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Both good and bad—but it's too early to say in what proportions

AS A rule, some people, such as Jacobins, tend to be more enthusiastic about revolutions than others, such as monarchs. Another fairly reliable rule is that revolutions abrupt enough to be associated with a single year (1642, 1789, 1848, 1917) tend to cause trouble but rarely bring lasting change. By contrast, revolutions gradual enough to be associated with a name (Renaissance, Reformation, Industrial Revolution) often do have enduring effects. A third rule, or hypothesis, might be that revolutions seem never to be entirely for the better or the worse, but somehow manage to combine both.

This survey has argued that society is in the early phases of what appears to be a media revolution on the scale of that launched by Gutenberg in 1448. This invites comparisons. There are Jacobins and monarchs to be found in both revolutions. In the first, the Jacobins were, by turns, printers, publishers, Protestants and writers; in today's revolution, the Jacobins tend to be those bloggers, vloggers and podcasters that bay for the blood of the odious “MSM” (mainstream media). As to monarchs, the first revolution had popes, monasteries and the real thing; today's revolution has, well, the MSM. Both revolutions are firmly in the category of gradualist, name-not-year revolutions.

That leaves benefits and evils. Gutenberg's revolution undoubtedly had enormous democratising effects. It enabled entire populations to read the Bible in their own language, liberating them from Latinate clergies that had kept them in superstitious serfdom. Further on in the revolution, people got news from far-flung corners of the world; one of the things that impressed Alexis de Tocqueville during his travels through America in 1831 was that even frontier families in remote Michigan had weekly newspapers delivered to their doorsteps. And the dramatically lower cost of disseminating the written word allowed many more people to express themselves creatively.

Each of these benefits also seems to have had a dark side. The availability of religious texts in the vernacular led to literalist and fundamentalist movements, and indirectly to religious wars. The

surge of textual expression produced not only classics but also pornography and propaganda. Printing presses reproduced “Mein Kampf” just as accurately as the Gospels.

Hell or heaven?

Against this backdrop, the big thinkers about today's media revolution tend to veer towards extremes of optimism or pessimism. Often the alignments are surprising. For instance, Michael Moritz, the venture capitalist who became famous for spotting both Yahoo! and Google, has a strongly pessimist streak. He worries about “amplification of the internet soapbox” and imagines what role user-generated media would have played in “1931 in Munich, how easy it would have been to broadcast the message; I think the Nazis would have got power quicker.”

Paul Saffo, a futurologist and one of the world's most enthusiastic technophiles, also looks at the downside. “Each of us can create our own personal-media walled garden that surrounds us with comforting, confirming information and utterly shuts out anything that conflicts with our world view,” he says. “This is social dynamite” and could lead to “the erosion of the intellectual commons holding society together...We risk huddling into tribes defined by shared prejudices.”

Now for the optimists: Lee Rainie, the director of the Pew Internet & American Life Project, a research foundation, believes that “people will become not less but more aware of differing arguments as they become heavier internet users,” because contradictory views are just a hyperlink away. A survey by Pew appears to confirm this view. Mr Anderson of “The Long Tail” says that “opinion is a marketplace, and marketplaces work when you have liquidity.” Liquidity is exactly what participatory media provide.

Some people worry about what the new media will do not only to democracy but also to brains, thoughts, grammar and attention spans. These concerns usually arise out of encounters with teenagers in their native habitat—ie, in front of screens with several simultaneous instant-messaging “threads” (“cu2nite bfz4evr”—“see you tonight and best friends forever”), besides iTunes and a video game running in the background, blogs in the foreground, and homework in the small window to the bottom right.

Other people are not worried at all. Steven Johnson, the author of “Everything Bad is Good for You”, argues that the very things about new-media culture that scare older generations actually make younger generations smarter, because participatory media train kids from an early age to sift through and discard clutter, thus “enhancing our cognitive abilities, not dumbing them down”.

Linda Stone, a former executive at both Apple Computer and Microsoft and now a consultant, argues that the affliction of “continuous partial attention” is in fact a hallmark of the era that is now ending, not the one that is starting. For the past two decades, Ms Stone thinks, many people have felt overwhelmed and anxious, constantly afraid that they could miss out on social opportunities if they concentrate on any one thing. This is now producing its own backlash, Ms Stone argues, because as people “long for protection and meaningful connections, quality over quantity”, they are “discovering the joy of focusing”.

Many new-media companies understand this, she says. Just as Google calms the chaos of the web with a clean white page, other companies are working on the filtering technologies that could—counter-intuitively, perhaps—make the era of participatory media more serene than the era of mass media.

The honest conclusion, of course, is that nobody knows whether the era of participatory media will, on balance, be good or bad. As with most revolutions, it is a question of emphasis. Generally speaking, people who have faith in democracy welcome participatory media, whereas people who

have reservations will be nostalgic for the top-down certainties of the mass media. Joseph de Maistre, a conservative who lived through the French Revolution, famously said that “every country has the government it deserves.” In the coming era, more than ever before, every society will get the media it deserves.

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Craig Newmark, Craigslist

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Dan Gillmor, Grassroots Media

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(see also a webcast by Jimmy Wales)

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Regulating business

The trial of Sarbanes-Oxley

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The corporate regulation brought in after the Enron scandal stands accused of making matters worse

Landov

DOWN in Houston the Enron trial proceeds apace. But far more significant for business, in America and beyond, than the fate of the energy company's former bosses is the outcome of another “trial” that is now at a crucial stage—that of the legislation introduced by Congress in 2002 in the wake of the Enron scandal.

The act was named after its two main sponsors, Senator Paul Sarbanes (pictured right above) and Congressman Mike Oxley (left). Sarbanes-Oxley, or SOX, as it has become known, was unpopular with business people from the start. In recent years it has been hard to find a chief executive of a public company who does not complain vehemently about the burdens imposed by the dreaded SOX. Indeed, rather than diminish as the initial shock wore off, the complaints have only got louder. The SOX-bashers have been joined by such luminaries as Alan Greenspan, the former head of the Federal Reserve and Bob Greifeld, the boss of the NASDAQ stockmarket. And the critics are not just American. Because of SOX, says Mr Greifeld, “international business clearly perceives a ‘problem’ with US markets today.”

SOX packaged together five different categories of reforms intended to protect investors from future Enrons. First, rules requiring better internal monitoring for potential fraud by a company's board and executives, including making the people at the top certify the quality of their firm's financial reports. Second, new measures to improve the monitoring of firms by relevant outside

professionals, such as lawyers and auditors, who got their own regulatory body, the Public Company Accounting Oversight Board (PCAOB). Third, more disclosure, including of a firm's internal-control structure. Fourth, new rules on the conduct of corporate insiders, such as a prohibition on loans to executives. Finally, new rules to ensure that securities analysts at banks operate independently from their firms' investment-banking activities.

SOX-bashers have found fault, to varying degrees, with all five reforms. Henry Butler, an economist, and Larry Ribstein, a law professor, set out the most comprehensive critique yet in a recent paper, “The Sarbanes-Oxley debacle: How to fix it and what we've learned”, which was presented at the conservative American Enterprise Institute. Describing SOX as a “colossal failure, poorly conceived and hastily enacted during a regulatory panic”, they argue (among other things) that the costs of implementing SOX are far higher than expected, both in cash terms, and even more so when they count the indirect costs—such as managers' reluctance to take risks because of the new “climate of fear” in the boardroom, and the missed opportunities of foregone investment. Although they admit that SOX may have reduced the risk of fraud, they argue that this benefit is far outweighed by the costs.

Messrs Butler and Ribstein would ideally like SOX to be repealed. But even if a court case challenging the constitutionality of the PCAOB (and by extension, SOX) is successful, it is more likely that Congress will simply amend the law.

All SOX critics agree that the top priority for reform is Section 404 of the law, which regulates the internal controls that firms use to reduce the risk of fraud or error in their financial statements. The burdens imposed by Section 404 are the main reason why formerly enthusiastic supporters of SOX, such as Mr Greenspan, are now demanding reform.

Section 404 has almost certainly improved the quality of internal controls at the firms where it has been implemented. But the question is not whether better controls lead to less risk—how could they not?—but whether that reduction in risk is worth the price. According to a recent study by CRA International, a research firm, in the first year of SOX implementation, for larger companies (with a market capitalisation of at least $700m), the average direct cost of Section 404 was $8.5m; for smaller public companies ($75m-700m), the average cost was around $1.2m. The SEC has not yet asked the very smallest public companies, with a value of less than $75m, to comply with Section 404.

The good news is that Section 404 costs are expected to fall by around 40% in the second year, says CRA, as the new system beds in. Even so, the costs are still higher than anyone expected them to be—the SEC initially forecast an average cost of $91,000 per company—and the burden is disproportionately heavy for smaller companies.

Much of the blame for this should be pinned on accounting firms, which, despite being seen by the public as big offenders in the Enron and WorldCom scandals, have emerged as the big beneficiaries from SOX. According to Joe Grundfest, a former SEC commissioner, the audit industry has several incentives to “push Section 404 compliance to a point of socially inefficient hyper-vigilance.” To avoid further damage to their reputations, and to minimise the risk that they will be sued over accounting irregularities, audit firms are adopting the most prudent possible interpretation of the Section 404 rules—rules that are vague and open to argument. And, as Mr Grundfest points out, the “more onerous the requirements of Section 404, the more money the audit profession can earn” by selling its services.

A couple of proposals could help tackle this problem, neither of which would require a wholesale reform of SOX by Congress. In a report due on April 23rd, the SEC's Advisory Committee on Smaller Public Companies was expected to recommend that companies be exempted from Section 404 if their market capitalisation is less than $128m and their revenues are under $125m. Firms

with a market value of up to $788m, and revenues of under $250m would be partially exempted.

This proposal has run into strong opposition, not least from Mr Sarbanes himself, who points out that it would “effectively exempt four out of every five companies”. True, but it was failures at big firms that gave rise to SOX, not at small ones, which investors have always thought riskier. In all, the exemption would cover firms accounting for only 6% of total American stock market value, leaving 94% of public companies by value still subject to Section 404.

Rather than exempt companies, Section 404 should be refined to make it more palatable for all firms, argues Robert Pozen, the head of MFS, a fund-management firm. At the moment, audit companies are looking at far too many internal controls—some 669 on average at the biggest firms, according to CRA—including items such as travel expenses and the handling of petty cash that are highly unlikely to have any serious impact on a company's financial reporting. Mr Pozen reckons that the SEC has the authority to require a narrower focus on those internal controls that look at material risks to a firm's financial reports.

Mr Grundfest goes further. As it stands, the PCAOB can penalise auditors that are too lax. He would like it to punish those audit firms that are over-zealous in their interpretation of Section 404, too. What could be fairer than that?

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The Enron trial

The grilling of Skilling

Apr 20th 2006 | HOUSTON
From The Economist print edition

A frustrating week for Jeffrey Skilling

IS THIS the same man who once flaunted a licence plate reading WLEC, for “World's Leading Energy Company”? Under cross-examination this week, the once-brash Jeffrey Skilling was mostly cool and respectful, despite spasms of testiness. The former chief executive of Enron, a bankrupt energy-trading company, insisted to a courtroom in Houston that he had “nothing to hide”, even as he faces 28 counts involving securities fraud, insider trading and false statements to auditors.

Sean Berkowitz, the government's bulldog-like prosecutor, produced a torrent of accusations. Among them: that Mr Skilling had manipulated the company's earnings to meet analysts' targets, using reserves from a “cookie jar”. If analysts wanted 33 cents per share, then that is what Enron would report, said Mr Berkowitz. In the second quarter of 2000, near the apex of Enron's fortunes, Mr Skilling has said he did tell another executive to “shoot for 34” cents a share but insists there was no manipulation. Mr Berkowitz also argued that Mr Skilling kept big problems and trading risks at Enron from investors—a charge Mr Skilling forcefully denied.

Reuters

Controls freak

As the “I do not recalls” mounted, Mr Berkowitz played up Mr Skilling's hazy memory. He grilled him about a tiny company called Photofete, run by a former girlfriend, which had dealings with Enron; Mr Skilling's estimate of how much he invested in Photofete was much too low, cheques showed. Far graver were questions about why Mr Skilling tried to sell 200,000 shares of Enron on September 6th 2001, just weeks after he had resigned from the company for “personal reasons”. Though this appears to be about a fifth of Mr Skilling's Enron shareholdings at the time, he claims not to remember the transaction, which was taped. (Soon thereafter he sold 500,000 shares, which he attributes to September 11th.) Mr Berkowitz also questioned why Mr Skilling, his ex-wife and girlfriend all sold substantial stock in the autumn of 2000.

So how did he do? For a self-confessed “controls freak”, Mr Skilling emerges, at best, as oddly unaware of his responsibilities and of the peculiar goings-on at his company, which he claims to have left in its “best shape” in 2001. “You're out of town, the lights are out,” said Mr Berkowitz sceptically of Mr Skilling's various explanations for why he was out of the loop. Mr Skilling will get a friendlier face next. His lawyer, Daniel Petrocelli, will re-examine him; then comes another chance for Mr Berkowitz, and some other defence witnesses. After that, Kenneth Lay, Mr Skilling's co-defendant, could take the stand next week. Then, the long-suffering jury—now in its twelfth week of immersion in off-balance sheet vehicles and hedging strategies—will decide their fates.

Software

Universal service?

Apr 20th 2006
From The Economist print edition

Proponents of "software as a service" say it will wipe out traditional software

SOMETHING momentous is happening in the software business. Bill Gates of Microsoft calls it "the next sea change". Analysts call it a "tectonic shift" in the industry. Trade publications hail it as "the next big thing". It is software-as-a-service (SaaS)—the delivery of software as an internet-based service via a web browser, rather than as a product that must be purchased, installed and maintained. The appeal is obvious: SaaS is quicker, easier and cheaper to deploy than traditional software, which means technology budgets can be focused on providing competitive advantage, rather than maintenance.

This has prompted an outbreak of iconoclasm. "Traditional software is dead," says Jason Maynard, an analyst at Credit Suisse. Just as most firms do not own generators, but buy electricity from the grid, so in future they will buy software on the hoof, he says. "It's the end of software as we know it. All software is becoming a service," declares Marc Benioff of salesforce.com, the best-known proponent of the idea. But while SaaS is growing fast, it still represents only a tiny fraction of the overall software industry—a mere $3.35 billion last year, estimates Mr Maynard. Most observers expect it to be worth around $12 billion by 2010—but even that is equal only to Microsoft's quarterly sales today. There is no denying that SaaS is coming. But there is much debate, even among its advocates, about how quickly it will grow, and how widely it will be adopted.

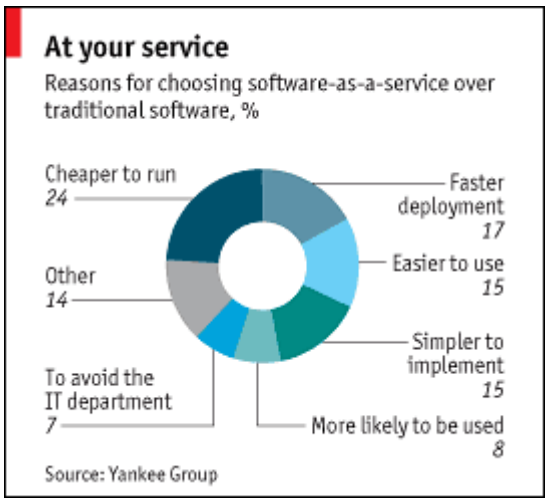
At the moment, small and medium-sized businesses are the most enthusiastic adopters of SaaS, since it is cheaper and simpler than maintaining rooms of server computers and employing staff to keep them running. Unlike the market for desktop software, which is dominated by Microsoft, or for high-end enterprise software, which is dominated by SAP and Oracle, the middle ground is still highly fragmented, which presents an opportunity. "This is the last great software market left—the last unconsolidated market," says Zach Nelson of NetSuite, which provides a suite of software services including accounting, sales-force automation and customer service. His firm is targeting small and medium-sized businesses by providing "verticalised" services—that is, versions of its software adapted to particular types of company, such as professional-service firms, wholesale distributors and software firms.

Large companies, says Mr Nelson, have already made big investments in traditional software. "They've already been through the pain," he says. So they will not be in a hurry to ditch their existing investments in traditional software from the likes of SAP and Oracle. "I have no fantasy of replacing those guys," says Mr Nelson. But Mr Benioff of salesforce.com disagrees. His firm provides customer-relationship management (CRM) software as a service, which is already used by many big firms including Cisco, Sprint and Merrill Lynch. "The world's largest companies are now using salesforce.com for the world's largest CRM implementations," he says. "It's the future of our industry that everything will be a service."

Even so, Mr Maynard reckons it will be some time before large companies fully embrace the service model. However, lingering concerns over security, reliability, archiving and regulatory

compliance will eventually go away, he believes, and basic functions—such as accounting, expense-management and human resources—will be switched over within five years. “How you handle accounts-payable doesn't determine your competitiveness,” he says. Eventually, only the bespoke software that provides competitive advantage to a firm will be left; everything else will be a service.

SaaS is fast becoming sophisticated and flexible enough to meet the needs of large companies, says Sheryl Kingstone of the Yankee Group, a consultancy, but “for the next five to ten years we will continue to have a mixture.” In a survey, she found that 81% of respondents leaned towards a “hybrid” model, combining traditional software with SaaS. Microsoft, Oracle and SAP are all belatedly moving into SaaS, but they understandably prefer to characterise it as a new model that will exist alongside the traditional way of doing things, and will appeal to some, but not all, customers.



So it is too soon to write the obituary for traditional software, even if its eclipse by SaaS seems to be only a matter of time. The SaaS market is growing by about 50% a year, compared with single-digit growth for traditional software, notes Mr Maynard. “It doesn't mean the big guys are going to die overnight,” he says, “but this is where the market is heading.”

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Executive pay

Raymond reviewed

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Why the outrage about Exxon misses the point

THE media have had a field day with the news that Lee Raymond, the retiring chairman of Exxon Mobil, received “compensation” worth at least $398m in his last year in charge of the oil giant. Headlines such as “Exxon chairman's $400m parachute” were everywhere, as editorials condemned what has become the latest “worst-case” example of executive greed running wild.

But Mr Raymond was not alone in being condemned this week, as hacks also took aim at the exercise of stock options last year worth $174m by Terry Semel, boss of Yahoo!, and at the $1.6 billion of unrealised profits on stock options held by William McGuire, the boss of the UnitedHealth group.

An embarrassed Mr McGuire has now recommended that UnitedHealth suspend most of its use of stock-based compensation—though he has yet to offer to hand back any of the money and has denied allegations that his stock-option awards were in any way improper.

Exxon's ex-boss has been characteristically unapologetic, however. Mr Raymond seems to think that he has actually earned the money—much of which is the result of various long-term incentive schemes and hardly counts as the “retirement package” it was reported to be.

What is more, he has a point. Exxon earned more in profit last year—over $36 billion—than any company has ever done before. True, Mr Raymond has had the good fortune to work in an industry that has benefited from the soaring oil price. But even allowing for that, Exxon under Mr Raymond has enjoyed a remarkable record of using its capital to earn high profits—one reason why it has easily outperformed most other large oil companies in terms of total shareholder returns.

And it is the shareholders, after all, who pay Mr Raymond—and who have done well out of Exxon themselves. The real executive compensation scandals are those cases when bosses do well, while their shareholders do not.

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Flextronics software

Barbarians go soft

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From The Economist print edition

The market for Indian IT and outsourcing firms gets even hotter

FROM his office in Gurgaon, a boom-town next to Delhi, the future looks rosy to Arun Kumar, boss of Flextronics Software Systems (FSS), and one of the architects of India's information-technology triumphs. Competition is emerging, but “the opportunity is so large”, that things seem set fair for the next five years at least. Kohlberg Kravis Roberts (KKR), most famous of American private-equity firms, seems to share his optimism. On April 16th it announced it was buying 85% of FSS from its owners, Flextronics, a contract manufacturer for the electronics industry, with its headquarters in Singapore.

The price—$600m in cash with a further $250m plus interest due in eight years' time—make this one of the largest deals yet in India's IT industry, and the biggest leveraged buy-out by a private-equity firm operating in India. In recent months there have been a number of takeovers of both IT firms and of those in the broader area of remote back-office services (“business process outsourcing”, or BPO). Last August Oracle, an American software giant, bought control of i-flex, India's largest exporter of software products—in its case, banking systems. In March RR Donnelly, a big American printing firm, agreed to buy OfficeTiger, a Chennai-based BPO firm, for a reported $250m.

These deals and KKR's purchase illustrate three trends. First is the expected growth of IT-outsourcing and BPO. Mr Kumar estimates that, just in FSS's niche—sophisticated software for the communications industry—there is a potential market of $100 billion a year, of which so far only $2 billion is being outsourced. His firm, which had 90 people in 1995, now has 6,100, 85% of them in India. Second, this optimism about business prospects is being translated into valuations that make suitors hard to resist.

Third is the recent availability in India of the huge resources of private-equity firms, looking for a home. This is KKR's first investment in India, although last year, in what it describes as the largest private-equity investment in history in a technology firm, it was part of a consortium that acquired SunGard, a big financial-software firm, which, like most such companies, has substantial operations in India.

For Flextronics, the sale represents a handsome return on an investment made only two years ago. FSS made the first of its names as Hughes Software. It was briefly acquired, in 2003, by Rupert Murdoch's News Corp. It found itself in the shopping basket that bought Mr Murdoch another Hughes company, DirecTV, an important part of his global television ambitions. Flextronics picked up the software arm in 2004 as News Corp divested itself of the bits of Hughes it did not want. Now Flextronics has said it wants to get back to its own knitting—“electronics-manufacturing services”—though it has also said it intends to hang on to its 15% stake in FSS.

For FSS, an orphan for a second time, one difficulty all this raises is nomenclature. Because of its

stature in the industry, neither its potential recruits nor its customers were bothered by its last change of name, from Hughes to FSS. Mr Kumar says some of his employees' families, however, less steeped in the business, were worried about the damage it might do to their relation's marriage prospects. This time, he has announced a competition to suggest a name. *The Economist*'s entry? “AsSweet.” (As in: “a software firm by any other name would smell...”)

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General Motors

Last-chance saloon

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General Motors tries to revive Saturn—its former great hope

Reuters

THE struggling Saturn division of General Motors is preparing a multi-billion dollar relaunch that could decide if there is a future for the marque—once GM's most innovative. The new investment is critical to Saturn, but is controversial inside the car company, where rival divisions, like Chevrolet and Buick, are worried about their own share of GM's shrinking pie.

Originally designed as the carmaker's response to Japanese competition, Saturn started in 1989. Conceived by GM's visionary but flawed former chairman, Roger Smith, it was originally created as a free-standing company, with its own headquarters, assembly plant and even a unique contract with the United Auto Workers union. That agreement was revolutionary for its day, yielding higher productivity in return for profit-sharing and more say in day-to-day operations. Although critics found the first Saturn cars unremarkable, the brand was brilliantly marketed—with a customer-friendly, no-haggle sales strategy.

But Saturn has gradually lost its lustre. More powerful brands within the GM empire ran rings round Saturn, starving it of the cash it needed to develop exciting new products. The few additional models Saturn got were always late and boring. So, while the marketing innovation meant sales soared from 74,493 in 1991 to a peak of 286,003 just three years later, Saturn soon began to lose altitude. Last year it sold just 213,657 vehicles. With critics pressing GM to eliminate some of its brands entirely, Saturn is vulnerable. So the decision to unveil three new additions to the range at this month's New York Auto Show could be Saturn's last chance.

The old idea of Saturn as a company within a company, designed to enliven the whole group, is long gone. Saturn workers today operate under GM's master labour contract; the head of the

division has been demoted to a mere marketing boss; Saturn products are now built wherever GM can find the capacity—and these days there is plenty of that. The only distinctive aspect that remains is the no-haggle sales strategy, which Joe Phillippi, chief analyst with the consulting firm, AutoTrends, Inc., still sees as Saturn's prime proposition. With an array of new products, he insists, “they finally have a chance.” But if GM really wants to make Saturn a success, the billion dollars it is investing now should be seen as only a start.

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Pharmaceuticals

Profitless prosperity

Apr 20th 2006 | CHICAGO
From The Economist print edition

The biotechnology industry needs to grow up

Get article background

EVERY industry has its big conferences, but biotechnology must host one of the largest. Some 18,000 scientists, businessmen, financiers and hangers-on descended upon Chicago recently for the annual Bio conference. The gathering boasted plenty of posh parties, high-flying political visitors and boozy nights out at blues bars. To judge by this expense-account fiesta, biotech certainly seems to enjoy a lot of easy money just now.

By some measures the industry is indeed booming. Its American stockmarket value is up tenfold over the past decade, to about $500 billion. Burrill and Company, an industry investment bank, estimates that $350 billion has been invested in biotech, nearly half of that in the past five years. Global revenues have risen from $23 billion in 2000 to more than $50 billion last year.

And what of profits? Best not to mention those. Thirty years after the biotechnology revolution began, the industry has yet to turn an aggregate profit (see chart). Take away the huge profits of a few success stories such as Genentech and Amgen (two Californian firms which together make up a third of the American industry's stockmarket value) and the picture darkens further. David Beier of Amgen estimates that the industry as a whole has lost $100 billion since its creation in the 1970s.

Gary Pisano, a professor at Harvard Business School, argues that biotech needs a radically different business model. He thinks its problems arise because “this is the first time that science is the actual business.” Traditional industries, such as aeronautics or pharmaceuticals, are in business to make products and science merely serves that end. By contrast, most biotech firms are start-ups that have no products and little clue about how to convert their wizardry into things they can sell.

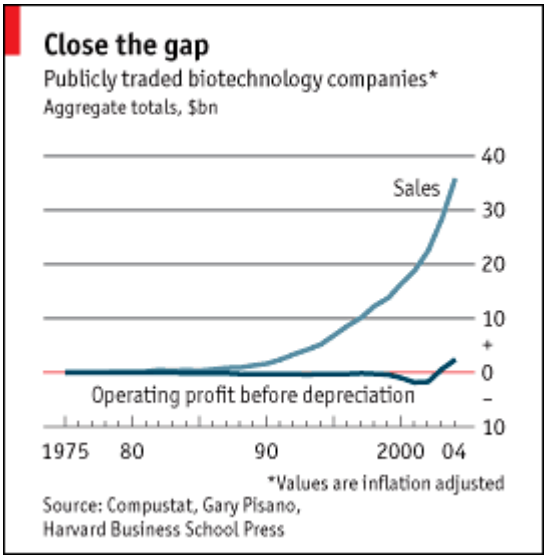
Few would deny that biotechnology has the potential to produce plenty of breakthroughs. Decoding the human genome has helped unlock some of the mysteries of the human body that biotechnologists are striving to turn into products. Optimists speak of drugs targeted to genetic subpopulations, and perhaps even personalised medicine. Firms such as Monsanto, Dow and DuPont are looking to biotech for better catalysts and enzymes, and working with food companies to produce healthier oils and tastier foods.

The trouble is that, after the bursting of a “biotech bubble” on the stockmarket a few years ago, investors are now understandably more discerning. Today's way of financing biotechnology, chiefly through the venture financing of start-up firms, looks unsustainable. On one plausible estimate, such early-stage investors are “holding the bag on 500 to 600 biotech firms they can't unload via public offering” on the stockmarkets. Frederick Frank, a vice-chairman of Lehman Brothers is

convinced that there will be a slow but sure shakeout in the industry in the coming years. Up to half of today's 1,500 or so biotech firms (fewer than 400 of which are public) will disappear, aided by mergers.

But if biotech companies are so far from breakthrough products, why will anybody buy them? The answer is that there is an industry in bigger trouble than biotechnology: conventional pharmaceuticals. Big drugs firms are hugely profitable today, but they fear for the future. Their product pipelines are often weak, tens of billions of dollars' worth of drugs will lose patent protection in the next few years, and generics are already eating away at margins.

So the big drugs firms are looking for the next big blockbuster drug under every possible rock—and the most promising rock is biotech. A new report by Ernst & Young, a consultancy, says that 2005 saw a big upsurge in mergers involving biotech firms, with Europe alone seeing 66 deals. Just this week, Novartis won final approval for its $5.4 billion takeover of Chiron, a biotech firm known for its cancer drugs and its blood-testing expertise. Novartis also runs its own start-up fund that invests in biotech firms. Daniel Vasella, the drug giant's chief executive officer, wants to keep his “hand on the technology edge” by keeping a close eye on, and acquiring, biotech companies. He reckons only a portfolio approach makes sense, since “there are 10,000 failures for each success—but when you win, you win big.”



Biotech firms sometimes sneer at big pharma as slow, bureaucratic and even stupid: “They're just barely smart enough to recognise genius,” sniffs one biotech man. But such posturing looks self-indulgent. The future may lie in a convergence of these industries with famously clashing cultures. John LaMattina, head of research and development for Pfizer, the world's largest drugs firm, insists that there is no big difference between biotech and pharma: “Molecules are molecules—I just don't buy this cultural argument.”

The convergence of big pharma and biotech also makes sense to Harvard's Mr Pisano, who sees a fundamental problem with the old financing model for biotech. Venture funds like to see quick returns, usually within five years, but the science involved often takes 15 to 20 years to come to fruition—if at all. He argues that biotech firms, which often pride themselves on their small size and freewheeling culture, need to grow up: “Size is key to integration of science, to learning and to manage risk.”

In the end, despite its paucity of profits, the biotechnology industry offers too much promise to be starved of funding. Burrill, the investment bank, estimates that it will attract some $35 billion in fresh investment in 2006. About $10 billion will come from joining up with big drugs firms and other integrated firms in alliances. The rest, reckons the bank, will come from the public equity markets.

Big Pharma plainly needs biotechnology, so those alliances make sense. But why would biotech be able to earn so much money on the stockmarket given its pitiful returns? Shreefal Mehta of Rensselaer Polytechnic Institute, an American engineering school, observes that there are always punters willing to gamble on very risky stocks in the hope of hitting the jackpot. The secret to biotech's future finances, he sums up, lies in “need and greed”. And perhaps, one distant day, in profits too.

Face value

A discreet dynamo

Apr 20th 2006
From The Economist print edition

Belgium has produced one of Europe's most interesting businessmen

AFP

THE country that plays host to the European Union, epitomises some of the worst features of Euro-sloth. Belgium's unemployment rate is 12.4%, among the highest in the EU; tax accounts for 55% of labour costs, the highest rate in the developed world. But behind the depressing economic statistics there remains enormous entrenched prosperity, as a casual drive around the luxurious suburbs of Brussels can confirm. And nobody epitomises the discreet wealth and continuing dynamism of European capitalism more than Albert Frère, a Belgian tycoon, who has recently turned 80—but continues energetically to re-shape corporate Europe.

Mr Frère is the only Belgian-born billionaire to feature in *Forbes* magazine's list of the world's 500 richest people. But he keeps himself well out of the limelight. He rarely gives interviews or speaks in public and bases himself in Gerpinnes, a small town in the southern Belgian rust-belt, near where he was born. This closeness to his roots might suggest a certain parochialism. In fact, few businessmen have more energetically embraced the idea of a borderless Europe. Mr Frère has had no compunction about selling some of the most famous names in Belgian business to foreigners. And despite his deliberately low profile, Mr Frère is attracting plenty of headlines these days, through high-profile deals in France and Germany.

As the biggest individual shareholder in Suez, a French water and waste company, he is a protagonist in discussions about the merger of Suez and Gaz de France, a French gas giant—a deal that is extremely politically sensitive, given France's devotion to economic nationalism. Mr Frère also recently amassed the biggest single stake in Lafarge, a French cement-maker with an uncertain future. And a few weeks ago he bought into Eiffage a French construction group. He was also involved with a move to take over Taittinger, one of the most prestigious champagne

producers—although this month he dropped out of the bidding.

Most of the recent attention, however, has focused on an announcement at the end of January by Groupe Bruxelles Lambert (GBL), a financial group controlled by Mr Frère, that it plans to sell some, or all, of its 25% stake in Bertelsmann, a German media conglomerate, on the stock exchange if market conditions are favourable. The Mohn family, owners of most of Bertelsmann, opposes a flotation, but the only way they can stop Mr Frère is by buying him out. He will probably use the €5 billion ($6 billion) or so raised in the sale of his holding in Bertelsmann to buy big stakes in companies in France and elsewhere.

Some predict that he will increase his stake of 8.2% in Lafarge to one-tenth or more of the company's equity and demand a board seat, to increase pressure on the company's management to work harder for shareholders. In anticipation of Mr Frère's likely demands, Bruno Lafont, the newish boss of Lafarge, recently unveiled a restructuring plan. Others think Mr Frère might increase his 6.1% stake in Eiffage to protect the company from unwanted advances from Sacyr Vallehermoso, a Spanish rival.

Mr Frère's record suggests that whatever he does will be shrewd. A self-made man and high-school drop-out, he has displayed impeccable timing in his wheeling and dealing. The son of a nail merchant, he started to buy up Belgian steelmakers in the 1950s and 1960s. By the time the Belgian government decided to nationalise steel companies in 1979, Mr Frère owned almost half of the industry.

Selling out worked well, since the steel industry was just entering a long and steep decline. Having pocketed a handsome sum, Mr Frère did not sit on the cash for long. He teamed up with Paul Desmarais, a Canadian entrepreneur, and others to buy GBL in 1982. The group owned stakes in Banque Bruxelles Lambert, Petrofina, a Belgian oil giant, and other big companies.

Once again, his timing was spot on. Mr Frère had acquired a significant stake in companies that had done well in Belgium's small and self-contained national market—assets that gained in value, as the EU moved towards a single European market. Over the past decade, he has sold what were once regarded as the crown jewels of the Belgian economy to companies in neighbouring countries. In 1997 he sold Banque Bruxelles Lambert to ING, a Dutch financial group. The next year Total, a French oil giant, bought GBL's stake in Petrofina. At that time AXA, a French insurer, bought GBL's stake in Royale Belge, a Belgian insurer. And last year he helped pave the way for the takeover of Electrabel, the biggest Belgian electricity company, by France's Suez.

Frère père

Perhaps unsurprisingly, given this record, Mr Frère sometimes seems to be more highly regarded in France than in his native Belgium. Although Belgium's King Albert II made him a baron in 1994 and he now has an entrée into almost all of the kingdom's boardrooms, he seems more comfortable with the French elite than at home. Spending long stretches of time in Paris in his flat in Avenue Foch, he has become a member of France's most selective business clubs. He is also a friend of Bernard Arnault, boss of Moët Hennessy Louis Vuitton, a big luxury conglomerate. In 1998 the two tycoons bought Château Cheval Blanc, one of France's best-known vineyards. Mr Frère is also a member of the Paris Jockey Club.

As with many ageing tycoons, the question of succession hangs over Mr Frère's business. In 1999 his younger son, Charles Albert, died in an accident. He has another son, Gérald, and a daughter, Ségolène, who are both involved in the family business. Gérald has taken over many of his father's responsibilities in Belgium, but he is said to be less keen on business than Frère senior. But those who know the older Frère say that he will never stop doing business. It is hard to deny

the lure of the next deal—especially when the last one served you so well.

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The oil industry

Steady as she goes

Apr 20th 2006 | BAKERSFIELD, CALIFORNIA, AND CALGARY, ALBERTA
From The Economist print edition

Why the world is not about to run out of oil

Getty Images

IN 1894 *Le Petit Journal* of Paris organised the world's first endurance race for “vehicles without horses”. The race was held on the 78-mile (125km) route from Paris to Rouen, and the purse was a juicy 5,000 francs. The rivals used all manner of fuels, ranging from steam to electricity to compressed air. The winner was a car powered by a strange new fuel that had previously been used chiefly in illumination, as a substitute for whale blubber: petrol derived from oil.

Despite the victory, petrol's future seemed uncertain back then. Internal-combustion vehicles were seen as noisy, smelly and dangerous. By 1900 the market was still split equally among steam, electricity and petrol—and even Henry Ford's Model T ran on both grain-alcohol and petrol. In the decades after that great race petrol came to dominate the world's transportation system. Oil left its rivals in the dust not only because internal-combustion engines proved more robust and powerful than their rivals, but also because oil reserves proved to be abundant.

Now comes what appears to be the most powerful threat to oil's supremacy in a century: growing fears that the black gold is running dry. For years a small group of geologists has been claiming that the world has started to grow short of oil, that alternatives cannot possibly replace it and that an imminent peak in production will lead to economic disaster. In recent months this view has gained wider acceptance on Wall Street and in the media. Recent books on oil have bewailed the threat. Every few weeks, it seems, “Out of Gas”, “The Empty Tank” and “The Coming Economic Collapse: How You Can Thrive When Oil Costs $200 a Barrel”, are joined by yet more gloomy titles. Oil companies, which once dismissed the depletion argument out of hand, are now part of the debate. Chevron's splashy advertisements strike an ominous tone: “It took us 125 years to use the first trillion barrels of oil. We'll use the next trillion in 30.” Jeroen van der Veer, chief

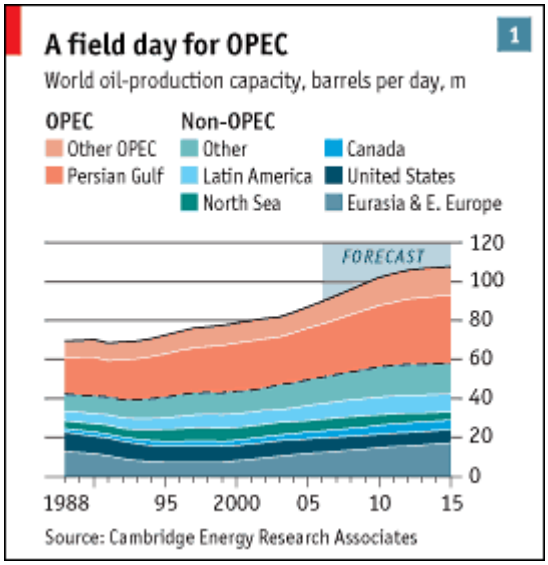
executive of Royal Dutch Shell, believes “the debate has changed in the last two years from 'Can we afford oil?' to 'Is the oil there?'”

But is the world really starting to run out of oil? And would hitting a global peak of production necessarily spell economic ruin? Both questions are arguable. Despite today's obsession with the idea of “peak oil”, what really matters to the world economy is not when conventional oil production peaks, but whether we have enough affordable and convenient fuel from any source to power our current fleet of cars, buses and aeroplanes. With that in mind, the global oil industry is on the verge of a dramatic transformation from a risky exploration business into a technology-intensive manufacturing business. And the product that big oil companies will soon be manufacturing, argues Shell's Mr Van der Veer, is “greener fossil fuels”.

The race is on to manufacture such fuels for blending into petrol and diesel today, thus extending the useful life of the world's remaining oil reserves. This shift in emphasis from discovery to manufacturing opens the door to firms outside the oil industry (such as America's General Electric, Britain's Virgin Fuels and South Africa's Sasol) that are keen on alternative energy. It may even result in a breakthrough that replaces oil altogether.

To see how that might happen, consider the first question: is the world really running out of oil? Colin Campbell, an Irish geologist, has been saying since the 1990s that the peak of global oil production is imminent. Kenneth Deffeyes, a respected geologist at Princeton, thought that the peak would arrive late last year.

It did not. In fact, oil production capacity might actually grow sharply over the next few years (see chart 1). Cambridge Energy Research Associates (CERA), an energy consultancy, has scrutinised all of the oil projects now under way around the world. Though noting rising costs, the firm concludes that the world's oil-production capacity could increase by as much as 15m barrels per day (bpd) between 2005 and 2010—equivalent to almost 18% of today's output and the biggest surge in history. Since most of these projects are already budgeted and in development, there is no geological reason why this wave of supply will not become available (though politics or civil strife can always disrupt output).



Peak-oil advocates remain unconvinced. A sign of depletion, they argue, is that big Western oil firms are finding it increasingly difficult to replace the oil they produce, let alone build their reserves. Art Smith of Herold, a consultancy, points to rising “finding and development” costs at the big firms, and argues that the world is consuming two to three barrels of oil for every barrel of new oil found. Michael Rodgers of PFC Energy, another consultancy, says that the peak of new discoveries was long ago. “We're living off a lottery we won 30 years ago,” he argues.

It is true that the big firms are struggling to replace reserves. But that does not mean the world is running out of oil, just that they do not have access to the vast deposits of cheap and easy oil that are left in Russia and members of the Organisation of Petroleum Exporting Countries (OPEC). And as the great fields of the North Sea and Alaska mature, non-OPEC oil production will probably peak by 2010 or 2015. That is soon—but it says nothing of what really matters, which is the global picture.

When the United States Geological Survey (USGS) studied the matter closely, it concluded that the world had around 3 trillion barrels of recoverable conventional oil in the ground. Of that, only one-third has been produced. That, argued the USGS, puts the global peak beyond 2025. And if “unconventional” hydrocarbons such as tar sands and shale oil (which can be converted with greater effort to petrol) are included, the resource base grows dramatically—and the peak recedes much further into the future.

After Ghawar

It is also true that oilmen will probably discover no more “super-giant” fields like Saudi Arabia's Ghawar (which alone produces 5m bpd). But there are even bigger resources available right under their noses. Technological breakthroughs such as multi-lateral drilling helped defy predictions of decline in Britain's North Sea that have been made since the 1980s: the region is only now peaking.

Globally, the oil industry recovers only about one-third of the oil that is known to exist in any given reservoir. New technologies like 4-D seismic analysis and electromagnetic “direct detection” of hydrocarbons are lifting that “recovery rate”, and even a rise of a few percentage points would provide more oil to the market than another discovery on the scale of those in the Caspian or North Sea.

Further, just because there are no more Ghawars does not mean an end to discovery altogether. Using ever fancier technologies, the oil business is drilling in deeper waters, more difficult terrain and even in the Arctic (which, as global warming melts the polar ice cap, will perversely become the next great prize in oil). Large parts of Siberia, Iraq and Saudi Arabia have not even been explored with modern kit.

The petro-pessimists' most forceful argument is that the Persian Gulf, officially home to most of the world's oil reserves, is overrated. Matthew Simmons, an American energy investment banker, argues in his book, “Twilight in the Desert”, that Saudi Arabia's oil fields are in trouble. In recent weeks a scandal has engulfed Kuwait, too. *Petroleum Intelligence Weekly* (PIW), a respected industry newsletter, got hold of government documents suggesting that Kuwait might have only half of the nearly 100 billion barrels in oil reserves that it claims (Saudi Arabia claims 260 billion barrels).

Tom Wallin, publisher of PIW, warns that “the lesson from Kuwait is that the reserves figures of national governments must be viewed with caution.” But that still need not mean that a global peak is imminent. So vast are the remaining reserves, and so well distributed are today's producing areas, that a radical revision downwards—even in an OPEC country—does not mean a global peak is here.

For one thing, Kuwait's official numbers always looked dodgy. IHS Energy, an industry research outfit that constructs its reserve estimates from the bottom up rather than relying on official proclamations, had long been using a figure of 50 billion barrels for Kuwait. Ron Mobed, boss of IHS, sees no crisis today: “Even using our smaller number, Kuwait still has 50 years of production left at current rates.” As for Saudi Arabia, most independent contractors and oil majors that have first-hand knowledge of its fields are convinced that the Saudis have all the oil they claim—and that more remains to be found.

Pessimists worry that Saudi Arabia's giant fields could decline rapidly before any new supply is brought online. In Jeremy Leggett's thoughtful, but gloomy, book, “The Empty Tank”, Mr Simmons laments that “the only alternative right now is to shrink our economies.” That poses a second big question: whenever the production peak comes, will it inevitably prompt a global economic crisis?

The baleful thesis arises from concerns both that a cliff lies beyond any peak in production and that alternatives to oil will not be available. If the world oil supply peaked one day and then fell away sharply, prices would indeed rocket, shortages and panic buying would wreak havoc and a global recession would ensue. But there are good reasons to think that a global peak, whenever it comes, need not lead to a collapse in output.

For one thing, the nightmare scenario of Ghawar suddenly peaking is not as grim as it first seems. When it peaks, the whole “super-giant” will not drop from 5m bpd to zero, because it is actually a network of inter-linked fields, some old and some newer. Experts say a decline would probably be gentler and prolonged. That would allow, indeed encourage, the Saudis to develop new fields to replace lost output. Saudi Arabia's oil minister, Ali Naimi, points to an unexplored area on the Iraqi-Saudi border the size of California, and argues that such untapped resources could add 200 billion barrels to his country's tally. This contains worries of its own—Saudi Arabia's market share will grow dramatically as non-OPEC oil peaks, and with it the potential for mischief. But it helps to debunk claims of a sudden change.

The notion of a sharp global peak in production does not withstand scrutiny, either. CERA's Peter Jackson points out that the price signals that would surely foreshadow any “peak” would encourage efficiency, promote new oil discoveries and speed investments in alternatives to oil. That, he reckons, means the metaphor of a peak is misleading: “The right picture is of an undulating plateau.”

What of the notion that oil scarcity will lead to economic disaster? Jerry Taylor and Peter Van Doren of the Cato Institute, an American think-tank, insist the key is to avoid the price controls and monetary-policy blunders of the sort that turned the 1970s oil shocks into economic disasters. Kenneth Rogoff, a Harvard professor and the former chief economist of the IMF, thinks concerns about peak oil are greatly overblown: “The oil market is highly developed, with worldwide trading and long-dated futures going out five to seven years. As oil production slows, prices will rise up and down the futures curve, stimulating new technology and conservation. We might be running low on $20 oil, but for $60 we have adequate oil supplies for decades to come.”

The other worry of pessimists is that alternatives to oil simply cannot be brought online fast enough to compensate for oil's imminent decline. If the peak were a cliff or if it arrived soon, this would certainly be true, since alternative fuels have only a tiny global market share today (though they are quite big in markets, such as ethanol-mad Brazil, that have favourable policies). But if the peak were to come after 2020 or 2030, as the International Energy Agency and other mainstream forecasters predict, then the rising tide of alternative fuels will help transform it into a plateau and ease the transition to life after oil.

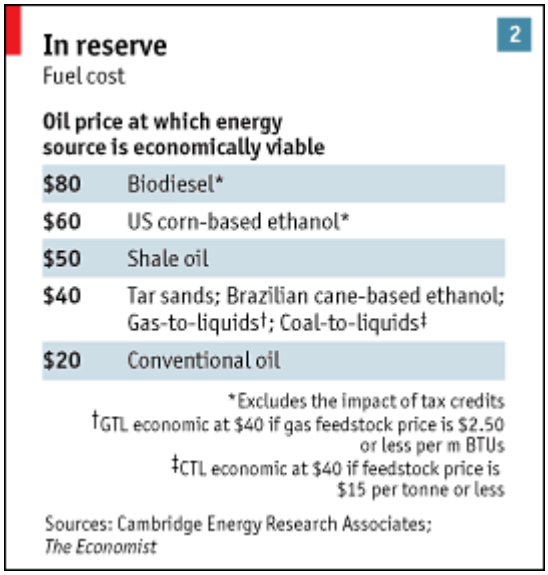
The best reason to think so comes from the radical transformation now taking place among big oil firms. The global oil industry, argues Chevron, is changing from “an exploration business to a manufacturing business”. To see what that means, consider the surprising outcome of another great motorcar race. In March, at the Sebring test track in Florida, a sleek Audi prototype R-10 became the first diesel-powered car to win an endurance race, pipping a field of petrol-powered rivals to the post. What makes this tale extraordinary is that the diesel used by the Audi was not made in the normal way, exclusively from petroleum. Instead, Shell blended conventional diesel with a super-clean and super-powerful new form of diesel made from natural gas (with the clunky name of gas-to-liquids, or GTL).

Several big GTL projects are under way in Qatar, where the North gas field is perhaps twice the size of even Ghawar when measured in terms of the energy it contains. Nigeria and others are also pursuing GTL. Since the world has far more natural gas left than oil—much of it outside the Middle East—making fuel in this way would greatly increase the world's remaining supplies of oil.

So, too, would blending petrol or diesel with ethanol and biodiesel made from agricultural crops, or with fuel made from Canada's “tar sands” or America's shale oil. Using technology invented in Nazi Germany and perfected by South Africa's Sasol when those countries were under oil embargoes, companies are now also investing furiously to convert not only natural gas but also coal into a liquid fuel. Daniel Yergin of CERA says “the very definition of oil is changing, since non-conventional oil becomes conventional over time.”

Alternative fuels will not become common overnight, as one veteran oilman acknowledges: “Given the capital-intensity of manufacturing alternatives, it's now a race between hydrocarbon depletion and making fuel.” But the recent rise in oil prices has given investors confidence. As Peter Robertson, vice-chairman of Chevron, puts it, “Price is our friend here, because it has encouraged investment in new hydrocarbons and also the alternatives.” Unless the world sees another OPEC-engineered price collapse as it did in 1985 and 1998, GTL, tar sands, ethanol and other alternatives will become more economic by the day (see chart 2).

This is not to suggest that the big firms are retreating from their core business. They are pushing ahead with these investments mainly because they cannot get access to new oil in the Middle East: “We need all the molecules we can get our hands on,” says one oilman. It cannot have escaped the attention of oilmen that blending alternative fuels into petrol and diesel will conveniently reinforce oil's grip on transport. But their work contains the risk that one of the upstart fuels could yet provide a radical breakthrough that sidelines oil altogether.


2
In reserve
Fuel cost
Oil price at which energy source is economically viable
$80 Biodiesel*
$60 US corn-based ethanol*
$50 Shale oil
$40 Tar sands; Brazilian cane-based ethanol; Gas-to-liquids†; Coal-to-liquids‡
$20 Conventional oil
*Excludes the impact of tax credits
†GTL economic at $40 if gas feedstock price is $2.50 or less per m BTUs
‡CTL economic at $40 if feedstock price is $15 per tonne or less
Sources: Cambridge Energy Research Associates; The Economist

If you doubt the power of technology or the potential of unconventional fuels, visit the Kern River oil field near Bakersfield, California. This super-giant field is part of a cluster that has been pumping out oil for more than 100 years. It has already produced 2 billion barrels of oil, but has perhaps as much again left. The trouble is that it contains extremely heavy oil, which is very difficult and costly to extract. After other companies despaired of the field, Chevron brought Kern back from the brink. Applying a sophisticated steam-injection process, the firm has increased its output beyond the anticipated peak. Using a great deal of automation (each engineer looks after 1,000 small wells drilled into the reservoir), the firm has transformed a process of “flying blind” into one where wells “practically monitor themselves and call when they need help”.

The good news is that this is not unique. China also has deposits of heavy oil that would benefit from such an advanced approach. America, Canada and Venezuela have deposits of heavy hydrocarbons that surpass even the Saudi oil reserves in size. The Saudis have invited Chevron to apply its steam-injection techniques to recover heavy oil in the neutral zone that the country shares with Kuwait. Mr Naimi, the oil minister, recently estimated that this new technology would lift the share of the reserve that could be recovered as useful oil from a pitiful 6% to above 40%.

All this explains why, in the words of Exxon Mobil, the oil production peak is unlikely “for decades to come”. Governments may decide to shift away from petroleum because of its nasty geopolitics or its contribution to global warming. But it is wrong to imagine the world's addiction to oil will end soon, as a result of genuine scarcity. As Western oil companies seek to cope with being locked out of the Middle East, the new era of manufactured fuel will further delay the onset of peak production. The irony would be if manufactured fuel also did something far more dramatic—if it served as a bridge to whatever comes beyond the nexus of petrol and the internal combustion engine that for a century has held the world in its grip.

Reshaping the IMF

Not even a cat to rescue

Apr 20th 2006
From The Economist print edition

The International Monetary Fund contemplates its future

WHAT is a firefighter to do when there aren't any fires? The IMF spent 1994-2002 dashing from one financial conflagration to the next. But the sirens have been silent for some time. As a result, the fund's budget is shrinking and the morale of its staff is sinking. Some of its best customers are now doing without it, leaving some of its biggest shareholders wondering what to do with it. In the run-up to the fund's spring meetings in Washington, DC, this weekend, its managing director, Rodrigo de Rato, has unveiled his proposals for a revamp. They range widely, from questions of power—of which emerging economies want more—to matters of paperwork—of which Mr de Rato wants much less.

Apart from generating reams of analysis, the fund's job is to furnish foreign exchange to countries that have temporarily run short. It can call on about $220 billion of hard currency in the first instance. That sounds like plenty. But some of its former customers now have big, shiny fire-engines of their own. South Korea, for example, has $217 billion in its vaults. Between them, eight East Asian countries (Japan, Singapore, Indonesia, China, Malaysia, the Philippines, Thailand and South Korea) command reserves worth about ten times the IMF total. These countries have even begun to pool a small fraction of their combined hoard, under what is called the Chiang Mai Initiative.

Lately no one has been calling on the fund's own supply. Brazil and Argentina have both repaid their debts. Only Turkey and Indonesia still owe it money on any scale. Quiet times are lean times for the IMF. Like any bank, it covers its running costs (which will amount to over $900m in the

year to April 2007) from the interest it earns on its loans. But this financing model “is no longer tenable”, Mr de Rato's report says. By its own projections, the IMF will live beyond its means by almost $300m in 2009-10. The belt-tightening this implies has not gone down well with staff, who show little taste for the austerity they are notorious for prescribing to others.

There are lots of ways to plug this gap (the fund sits on 103m ounces of gold, for example). But is the fund worth the price? Friends and foes alike urge it to recover its standing by rediscovering its roots. It was set up in 1944 to police exchange rates and to oversee the orderly resolution of trade imbalances. America's Treasury thinks at least one currency, China's yuan, warrants a bit of policing today, and many others think that America's $800 billion current-account deficit needs work.

But the fund's authority does not match this ambition. John Maynard Keynes envisaged his brainchild as a “grandmotherly” institution, able to guide and chide national governments. But the fund now has little sway over family members who do not need its money.

With no way to punish offenders, the fund is left only with the power of “surveillance”: keeping an eye on the policies and frailties of its members and reporting on each in turn. But several critics, including Mervyn King, the governor of the Bank of England, and Edwin Truman, of the Institute for International Economics, a Washington think-tank, argue that the fund should take a more panoramic view, examining its members collectively, not just one by one. Otherwise, it will miss the spillovers from one country to the next.

If the IMF were to wither away—its money untapped, its advice unheeded—should anyone care? If emerging economies want to insure themselves against financial crises, rather than run to the fund, surely they should be applauded? Alas, their self-reliance is expensive and inefficient—as if every home had its own fire-engine. Emerging economies are, in effect, lending to foreigners (by piling up treasury bonds paying miserable rates of interest) in order to underwrite borrowing from them (at higher rates of interest). According to Dani Rodrik, of Harvard University, the developing world's reserves carry an opportunity cost of nearly 1% of GDP.

One way for a country to narrow these costs is to seek a fatter return on its reserves. Larry Summers, Harvard's departing president and a former treasury secretary, thinks the IMF could offer its services as an international fund manager, pooling official reserves in a more rewarding portfolio of assets. But this idea may mistake the origins of the problem. The build-up in reserves reflects a lasting anxiety about financial markets, but also a lingering distrust of the IMF. Mr Summers assumes that countries will be willing to entrust their dollars to the IMF. But if they had that much confidence in the fund, they might not feel the need to accumulate quite so many reserves in the first place.

Worth weighting for

Members' contributions to the IMF, % of total

	Actual quotas	Implied by existing formula	Share of world GDP, 2001-03*
United States	17.38	17.24	31.79
Japan	6.23	7.19	12.51
France	5.03	4.27	4.53
China	2.98	5.07	4.46
Netherlands	2.42	2.77	1.32
Belgium	2.16	2.20	0.78
Mexico	1.21	1.86	1.92
South Korea	0.76	2.23	1.64
Malaysia	0.70	1.32	0.29
Thailand	0.51	0.87	0.39
Turkey	0.45	0.66	0.57

Source: IMF

*Three-year average of GDP at market exchange rates

How can the fund regain the confidence of its estranged members? The first step, as Mr de Rato recognises, is to give them a greater say in its affairs. The fund is close to being a shareholder democracy: the votes a country wields are proportional to the money it contributes. This “quota” is in turn meant to reflect a country's weight in the world economy. Even by the obscure formula that the fund uses, several emerging economies are now hugely underrepresented and many European countries overrepresented (see table).

Countries guard their quotas jealously. But Mr de Rato hopes they will agree to give a handful of the bigger emerging economies (China, Mexico, South Korea and Turkey) more votes, even if there is no appetite for a general increase in shares. Last year, Burhanuddin Abdullah, governor of Indonesia's central bank, warned that without changes, the “fund's credibility will continue to be undermined due to the monopolistic behaviour of large countries with veto power.” That power shows up in telling ways. Thomas Oatley and Jason Yackee, of the University of North Carolina, Chapel Hill, have shown that the fund's biggest rescue packages go to countries where the exposure of American banks is the greatest.

For all its mystique, the fund is at bottom just a financial middleman, as Michael Dooley, of the University of California, Santa Cruz, has pointed out. As such, it is always hemmed in by the threat of disintermediation. Countries such as Japan, China and South Korea can either lend to their neighbours through the fund, or they can bypass it and lend to their neighbours directly. Giving Asian countries a greater stake in the fund would encourage them to make use of it.

Mr de Rato also hopes to tempt them by changing the way the fund lends. Rather than mounting ad hoc rescue missions after the event, it would commit itself in advance to help favoured countries if the need ever arose. Which countries would qualify? Answer: those members pursuing sustainable policies that are nonetheless vulnerable to self-fulfilling reversals of sentiment on the part of their creditors. For such countries, a promise to lend might in itself avert the need ever to do so.

But could the fund ever revoke that promise? Disqualifying a strayed country might in itself precipitate a crisis, which is one reason why Barry Eichengreen, of the University of California at Berkeley, thinks the idea is a blind alley. On the other hand, if favoured countries can never fall from grace no matter what they do, the fund might find itself lending in support of unsustainable policies after all.

These objections need not be fatal. Moral hazard is part of all insurance arrangements. And as Michael Mussa, of the Institute for International Economics, has pointed out, the fund differs from an insurer in one important respect: the money it provides in a crisis has to be repaid. As long as governments care about the burden of repayment on future taxpayers, they will not seek loans capriciously.

By the time Mr de Rato's welcome proposals are enacted, if they ever are, the fund's identity crisis may well have resolved itself. If China slows, America starts saving again or interest rates spike, indebted or illiquid economies will struggle once again. Firemen with no blazes to put out are easily bored. Sadly, the fund's morale will not be this low for ever.

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Industrial loan companies

Resisting Wal-Bank

Apr 20th 2006 | NEW YORK
From The Economist print edition

A giant retailer's bid for a banking licence reopens old questions

WHEN Wal-Mart rolls into town, small shopkeepers quake. Now that the world's biggest retailer wants to enter the financial business, America's bankers are trembling, too. On April 10th the Federal Deposit Insurance Corporation (FDIC), one of America's bank regulators, held the first day of public hearings on Wal-Mart's bid to open an industrial loan company (ILC). Another hearing is due to take place on April 25th. An ILC licence would allow the mighty retailer to offer banking services along with its cheap lawnmowers, DVD players and groceries. The prospect of this brought bankers, trade unions and community activists to the hearings to voice their opposition.

Wal-Mart testified that it “is absolutely and unequivocally committed not to engage in branch banking.” It insists it wants an ILC only to save money on processing the 140m credit-card and other transactions it pays banks to handle each year. The retailer points out that local banks run branches in 1,150 of its stores, with 250 more to come—a sign that it sees these banks as partners, not rivals.

None of this has mollified the opposition. It believes Wal-Mart has bigger ambitions: in the past six years the retailer has tried (unsuccessfully) to buy banks in California and Oklahoma, and go into partnership with a Canadian bank. They fear that if the FDIC approves Wal-Mart's application, nothing will stop the retailer from entering banking in a few years' time. This, they say, is a risk too big to take.

But a risk for whom? Some opponents told the FDIC that a bank owned by a company of Wal-Mart's size might engage in anti-competitive behaviour or destabilise the economy. However, ILCs owned by General Motors and General Electric, also gigantic companies, and Target, another retailer, have done no such damage. And if Wal-Mart sticks narrowly to credit-card processing, as it says it will, its ILC will be less “bank-like” than many others.

The dispute may be partly about protecting consumers or helping the economy, but it is also about Wal-Mart itself. Banks want to protect their turf. And the company's size, success and ways of doing business have won it some vocal enemies. More broadly, however, the fight raises bigger questions about regulating America's banks.

ILCs first appeared around 100 years ago, as small, state-chartered banks that provided loans to industrial workers on low incomes who were shunned by traditional banks. They have remained largely exempt from America's 50-year ban on banks being owned by commercial companies. Since 1987, despite a tightening of the loophole, their number has grown rapidly even though ILCs are now chartered in only seven states (mainly Utah, California and Nevada). Between 1987 and 2005, ILCs' assets rocketed from $3.8 billion to more than $150 billion. The assets of the biggest, owned by Merrill Lynch, topped $60 billion. The number of Utah-chartered ILCs has more than doubled since 1997.

The growth of ILCs has raised two connected concerns. The first is that ILCs allow firms to skirt the separation of commerce and banking. The reason for the division is a fear that banks lend to their industrial affiliates at preferential rates, say, or discriminate against affiliates' competitors. Worse, in times of financial distress, the non-bank owner could raid a bank's deposits, causing a run on the bank—not to mention a claim on taxpayers' money through the FDIC, which insures deposits.

Anil Kashyap, an economist at the University of Chicago, thinks that proper regulation, which ensured all transactions between a bank and its affiliates were at “arm's length”, would prevent such difficulties. Markets, too, would discipline errant banks: any institution with a reputation for giving its parent sweetheart deals or discriminating against its competitors would not remain profitable for long.

Peter Wallison, of the American Enterprise Institute, a conservative think-tank, believes that the separation of the “suppliers of credit”—ie, banks—from the “users of credit” is an increasingly arbitrary one. He points to bank deregulation in 1999, which allowed non-bank financial companies (insurance firms, brokers and the like)—big users of credit—to own banks for the first time since the Depression. Mr Wallison argues that letting an insurer own a bank is little different from letting a retailer do so: the same conflicts arise, which can be managed with proper regulation.

The second question raised by Wal-Mart's application is whether ILCs are properly regulated now. As state-chartered banks, they are overseen by the FDIC rather than the Federal Reserve, which watches financial companies that control banks. The problem with this, argue some (including the Fed), is that only the Fed has broad powers to examine a bank's parent and its non-bank subsidiaries and act to stop problems elsewhere spreading to the insured bank. On this logic, ILCs belong in the Fed's purview. Not suprisingly, the FDIC disagrees.

These concerns have been heightened by two bills before Congress that would make ILCs even more popular. One bill would allow them to open branches across America. The other would let them offer interest-bearing chequebook accounts to business customers. Critics of ILCs say that fundamental questions of bank regulation are at stake, which deserve a thorough airing in Congress: they should not be settled piecemeal, by single bills and licences.

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Property derivatives

Homes with hedges

Apr 20th 2006 | CHICAGO
From The Economist print edition

Applying modern finance to America's biggest asset class

THERE are many ways to manage risk in America's markets, but the country's sophisticated web of financial products has a $21.6 trillion hole in it. That is how much wealth is tied up in residential property—far more than even the $15 trillion value of America's publicly traded equities. And unlike investors in shares, bonds and many other assets, those with a stake in housing do not have an easy way to hedge the risks. However, the Chicago Mercantile Exchange (CME) is planning to fill that gap.

In the next few weeks, the CME is likely to open trading in financial futures and options linked to American house prices. Investors who want to hedge the risks of residential property—or merely to speculate on the market's direction—will be able to bet on a rise or drop in a house-price index, without having to buy or sell bricks and mortar. With interest rates on the rise, prompting worries that the recent housing boom is about to give way to a downturn, the potential appeal of these new hedging products is easy to see.

Punters will be able to bet on price changes in ten cities from Boston to San Diego, as well on a national index that aggregates all ten. The indices will be part of the CME's Alternative Investment Products group, which fosters derivatives linked to economically important trends and events not directly related to underlying securities or commodities. The group already has products based on the weather and on economic data such as non-farm payrolls.

Creating a useful and reliable index of house prices is tricky, since no two homes are identical and the market is full of messy transactions. But a pair of economists, Karl Case and Robert Shiller, have spent more than a decade sorting out many of the problems, and for several years have published proprietary indices that highlight trends in the market. (Mr Shiller, a tauricidal academic who has spent much of his career slaying bulls and their foaming theories, has a special interest in tracking American house prices, which he has claimed are ripe for a fall.) The Case-Shiller indices have now been tweaked a bit to create a version suitable for trading.

Because the new derivatives will allow bets up to only a year ahead, homeowners will not be able to use them to hedge long-term risks. That limits their usefulness for ordinary folk. For many companies in the property industry, however, they should be helpful. A property developer or contractor, for example, can start a housing project without worrying whether prices will fall sharply by the time it is completed. Monika Piazessi, an economist at the University of Chicago's Graduate School of Business, says that half the volatility in the price of individual homes is linked to city-wide changes in prices. So the CME's new city indices could go a long way towards lowering the risks.

Financial firms such as mortgage lenders will also no doubt find uses for the new derivatives. And so will investors with a view about America's residential property market—whether they expect a

continued boom, or a bust.

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Credit derivatives

The tender age

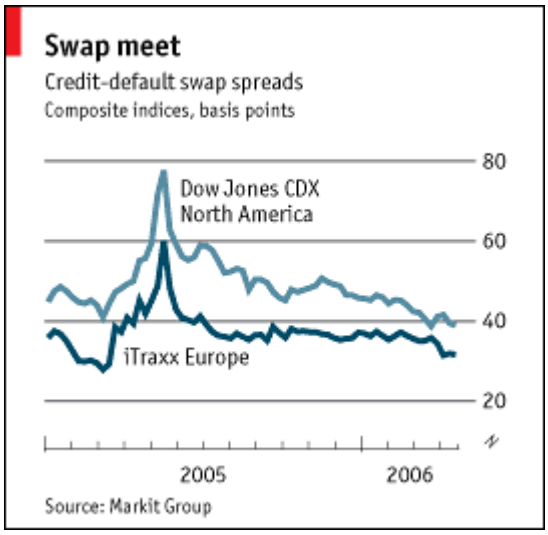
Apr 20th 2006
From The Economist print edition

Unexpected twists in the booming market for credit-default swaps

THE past few months have been trying for buyers of credit derivatives. They include banks and hedge funds that have acquired credit-default swaps (CDSs), the cornerstone of the market. This still young area of the financial world now consists of contracts worth $17 trillion, more than all the world's outstanding corporate debt. A credit derivative provides insurance if a borrower goes bust—or a means to bet that it will do so. Lately, a few of those bets have gone spectacularly wrong.

First, hardly any companies went under in the first quarter. Rating agencies say that the number of defaults is the lowest for almost a decade. Though good news for companies, it is bad for owners of swaps. Meanwhile, analysts report a sharp rise in the number of CDS contracts being written. All this has lowered the premium, or spread, on credit derivatives (see chart). Those who own protection have lost money (although sellers have benefited).

But the issue that has most hurt credit-derivatives buyers, analysts say, is an arcane and technical one. A few companies have unexpectedly tendered for their own bonds. Because buy-backs eliminate the risk of default, the consequences for the price of CDS contracts written on these bonds have been uniformly brutal.



The companies include J. Sainsbury, a British supermarket chain, which last month bought back all £1.7 billion ($3.0 billion) of its outstanding bonds in order to cut its financing costs. That meant no “deliverable” debt was left to be insured—it was replaced by mortgage-backed securities in two new entities, named after Britain's Longstone and Eddystone lighthouses. CDS investors have ended up on the rocks. Last year, when Sainsbury was struggling, some of these swaps were priced at 150 basis points per unit of debt insured. Now they fetch around 20.

Something similar happened at TDC, a Danish telecoms company acquired last year in Europe's largest leveraged buy-out so far. CDS premiums written on its bonds, which had been expected to soar, plunged when TDC declared that it would redeem its bonds at par as part of the deal.

In America panic among CDS buyers has been rarer. But a restructuring at Cendant, a diversified travel, leisure and property group, created deep confusion and a sharp drop in CDS premiums last month. It is expected to tender for its bonds as it breaks itself up into four units.

In each case, holders of CDS contracts suddenly found themselves committed to paying for protection on bonds on the verge of extinction—rather like paying for insurance on a car heading for the scrapyard. According to Jon Jonsson, European credit-derivatives strategist at Merrill Lynch, they were particularly caught by differences between European and American corporate law.

As a result, the International Swaps and Derivatives Association is investigating whether standard CDS documents may need changing to incorporate the risks from reorganisations or leveraged buy-outs. “There are a host of these we can see in the pipeline,” says Kimberly Summe, ISDA's general counsel.

Of course, what's bad for buyers is good for sellers. But such technical disruptions undermine confidence for everyone. As the IMF pointed out recently, the credit-derivatives market helps to steady the financial system. It enables banks to offload credit risk, provides transparency on lending conditions and may even smooth the ups and downs of the credit cycle.

The secondary market, however, is prone to worries about liquidity and bouts of panic. Panic is an understandable reaction for buyers who suddenly find that their insurance contracts are worthless. Now they have at least been warned.

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Leveraged debt

Going naked

Apr 20th 2006 | NEW YORK
From The Economist print edition

Covenants that once protected lenders are becoming notable for their absence

DEBT has been so cheap for so long in America that new underwriting for a company with a catastrophic balance sheet on terms once reserved for the most prudent raises barely a shrug. What has caused a few splutters recently is more subtle: the great flood of liquidity has washed away the tight operating restrictions that banks once demanded for financing highly leveraged deals.

Shifts in the structure of loans are harder to track and understand than are changes in interest rates, but they are just as important. Ideally, lenders want not only rates commensurate with risk, but also controls that confine risk and maybe even provide an escape hatch. In the past these protective covenants came in two forms. The first limited a company's ability to weaken its balance sheet voluntarily—say by paying large dividends or by making acquisitions. The second allowed banks to watch borrowers' performance and to step in before a collapse looked likely. Banks could declare a company to have defaulted if its ratio of cashflow to debt-service payments, debt to equity, expenses to revenues, or some other measure fell outside specified limits.

The fortunes of two department-store chains show just how times have changed. Retailers were among the first to embrace leveraged buy-outs when the trend first caught on in the 1980s. Macy's, a New York landmark, has the dual distinction of being the subject of one of the first big deals, when it was transformed from a public to private company in 1986, and of being one of the first to fail, when it filed for bankruptcy in 1992. A roomful of bankers pulled the trigger, having watched Macy's miss one target after another.

Contrast this with last October's buy-out of Neiman Marcus, a Dallas icon and a rival of Macy's, led by Texas Pacific and Warburg Pincus, two private-equity firms. Buy-outs are now routine. What was not routine was the lack of conditions tied to the deal, says Paddy Hirsch, senior editor of Standard & Poor's LCD, a firm that tracks the leveraged-loan market. Some $2 billion of the $5.1 billion buy-out came as bank debt, yet covenants were almost entirely absent. If the loan comes apart, Mr Hirsch says, it will be because it can't, or won't, be repaid, not because bankers decide the lending terms are being broken. Meanwhile, Neiman will be free to do what it likes with the cash at its disposal.

Since October there have been several similar deals, says Mr Hirsch. On April 13th Dole Food, a private company that is the world's largest seller of fresh fruit, issued $750m in bank debt. It did agree to a few restrictions, such as a limit on further debt, but there are no conditions about monitoring the company's health. Only 18 months ago Chiquita Brands, another fruit firm which has a slightly better credit rating, issued debt at a higher price (275 basis points over LIBOR, against 175 for Dole). The deal was swaddled in covenants covering, among other things, the European Union's farm-trade policies and the commercial viability of selling pre-washed lettuce.

So, too, in the media industry. Last month Cablevision, a New York operator with a costly hobby of mismanaging the local professional basketball team and which has had to seek covenant waivers in the past, arranged a $3.5 billion loan with few covenants at 175 basis points over LIBOR. At the end of 2004 Mediacom, an Iowa cable company with a similar credit rating, paid 250 basis points over LIBOR for a $500m loan packed with covenants. If things go well, of course, covenants are irrelevant. But if not? “These deals will sink like a stone,” says Mr Hirsch.

Why have lenders lost interest in covenants? One explanation is that, as bank loans begin to trade in the secondary markets like ordinary bonds, the banks themselves are less interested in preventing borrowers from imploding than when they kept the debt on their books. Another is that the debt market is temporarily frothy. Mr Hirsch says there was a similar change in lending terms before the meltdown of 1998, though even then lenders earned much wider spreads. Some old hands are taking note. Many of the insurance companies and specialised institutions that used to buy these loans are now out of the market, replaced, Mr Hirsch says, by hedge and mutual funds. Must be a brave bunch.

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Piracy insurance

For those in peril

Apr 20th 2006
From The Economist print edition

The world's insurers are taking a more serious look at robbery on the sea

TO THOSE safely on dry land, pirates may seem to be figures from Hollywood or the history books. Those at sea know better. Pirates still prey on ships and sailors. And far from being jolly sorts with wooden legs and eye patches, today's pirates are nasty fellows with rocket-propelled grenades and speedboats.

According to the International Maritime Organisation, 266 committed or attempted acts of piracy were reported last year. Although this was a lower figure than in 2004, in part because many small-time pirates died in that December's tsunami, risk experts say that a more brazen, violent and organised strain has emerged. Pirates are said to have injured or assaulted 152 crew in 2005; they abducted 652, of whom 11 are still missing. They hijacked 16 ships; a tug and a barge are unaccounted for.

Because pirates go where the pickings are best, some of the busiest shipping areas, including the South China Sea and the Malacca Strait, are among the world's most dangerous waters. Oil regions can also be risky: pirate attacks off the coast of Nigeria have increased markedly. Iraq, too, has seen a rise in maritime violence. “This is a target-rich environment,” says Dominic Armstrong of Aegis, a security-risk consulting firm in London. Because ships' crews are usually unarmed, he adds, “they're completely vulnerable.”

Ships plying risky waters are charged higher insurance premiums, which are ultimately passed on to businesses and consumers. One of the biggest marine-insurance pay-outs in recent years—about $70m—stemmed from the 2002 attack on the *Limberg*, a French tanker, off Yemen. Even so, piracy business is a small fraction of the more than $12 billion in marine premiums written annually.

Risk experts say that the lines between piracy and terrorism are blurring. Reflecting the trend, a committee of marine underwriters at Lloyd's, the London insurance market, recommended recently that piracy risk be shifted from inclusion in standard policies covering physical damage to boats to war-risk policies.

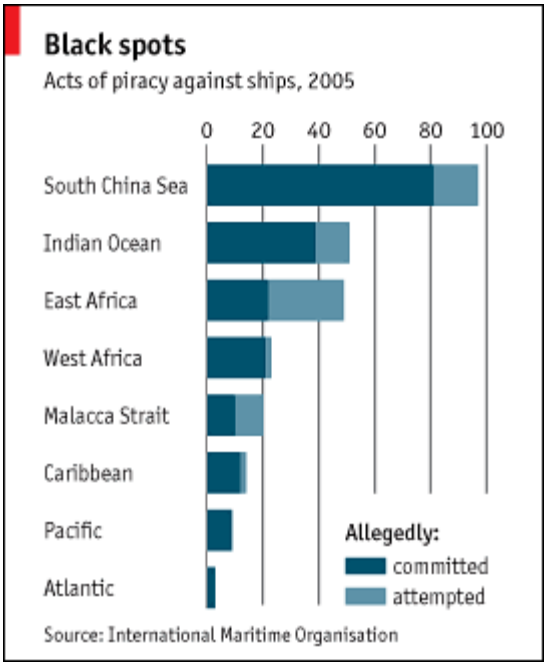
Sceptics say that this will simply allow insurers to charge more for coverage in a highly competitive marine market. Marine underwriting has generally been unprofitable in recent years, as insurers have slashed rates to win custom.

Piracy is a risk for vessels of all sorts. Yachts, tankers, even a United Nations ship carrying rice for victims of the tsunami have been attacked in the past year. Most worrisome was an attack last November on the *Seaborne Spirit*, a cruise ship bound for the Kenyan port of

Mombasa with more than 300 people aboard, which was hit by armed men off the coast of Somalia. The assailants were driven off by a security system that repelled them with a sonic blast, but only after they had blown a hole in the ship and injured a crewman.

Pirates are after everything from cargo (palm and vegetable oil are considered especially easy to dispose of) to ransom money or even the ships themselves: the booming Chinese economy has created such a demand for vessels that a market for second-hand ships has developed.

The attacks show no signs of abating. The Piracy Reporting Centre, which tracks such incidents around the world, says that there were 41 attacks, attempted and successful, between mid-March and mid-April off Somalia alone. For many, life on the high seas remains perilous.



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Economic focus

Money to burn

Apr 20th 2006
From The Economist print edition

Why oil exporters' enormous surpluses may last longer this time

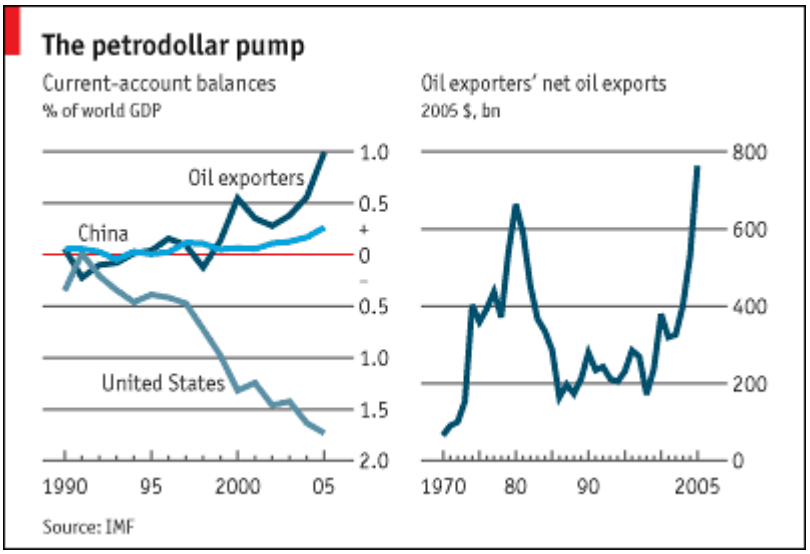
PLENTY of Americans blame unfair competition from Asia, and especially China, for their country's gigantic current-account deficit. Yet the group of countries with the world's biggest current-account surpluses is no longer emerging Asia, but exporters of oil. As the price of their chief resource has climbed—this week it hit a new nominal record price of more than $70 a barrel—these economies have enjoyed a huge windfall. From an American point of view, the rise in oil prices has explained half of the widening of the current-account deficit since 2003, a bigger share than that accounted for by China.

A timely chapter in the International Monetary Fund's latest *World Economic Outlook*, published this week, explores the implications of these gushing petrodollars for the world's current-account imbalances. Thanks to higher prices and increased production, the revenues of oil exporters—members of the Organisation of Petroleum Exporting Countries (OPEC), plus Russia and Norway and a few others—reached almost $800 billion in 2005. Adjusted for inflation, this beats the previous peak in 1980; and in the past three years real oil revenues have risen by almost twice as much as in 1973-76 or 1978-81. In relation to world GDP, however, revenues have increased by only a little more than during those earlier price shocks.

The oil exporters' current-account surpluses reached almost $400 billion last year, more than four times the total for 2002, and are forecast to rise to $480 billion in 2006. The combined surpluses of China and other emerging Asian economies were only $240 billion last year. Oil exporters' surpluses are also much bigger relative to the size of their economies, averaging 18% of GDP last year, twice as much as at the previous peak in 1980, and much more than China's surplus of 7% of GDP.

Petrodollars can be recycled to oil-importing economies in one of two ways. Either oil exporters can import more goods and services, or they can invest their windfalls in global capital markets, thereby financing the current-account deficits of America and other oil importers. Whether the exporters spend or save their revenues determines the path of global imbalances, including America's vast deficit.

After previous increases in oil prices, current-account imbalances have tended to adjust fairly swiftly, through three main channels. First, higher oil prices reduced real incomes and profits in importing countries, squeezing domestic spending and hence imports of both oil and other goods. Second, as oil prices pushed up inflation, central banks raised interest rates, which further slowed domestic demand and so trimmed the external deficit. And third, importers' real exchange rates fell, helping to bring their current accounts back towards balance. Conversely, exporters' surpluses were reduced by stronger domestic demand (and hence imports) and rising real exchange rates.



The IMF suggests that this time may be different, with the oil producers' surpluses persisting for longer than in the past. Oil exporters have spent a smaller share of their latest windfall on imports of goods and services than during previous oil shocks. Since 2002 they have spent barely half of their extra revenues, compared with three-quarters in the 1970s. Past windfalls typically encouraged wasteful budgetary blow-outs, leaving government finances in trouble once oil prices fell back. This time governments are being more cautious, even though the futures markets expect oil prices to stay high.

America gains little, in terms of its current-account balance, even from the imports that oil exporters do buy. It now accounts for only 8% of OPEC countries' total imports; the European Union has 32%. So even if the exporters spent all their extra revenue, America's current-account deficit would increase as oil prices rise. This partly explains why in recent years the EU's trade balance with the oil exporters has barely changed even as America's deficit has grown sharply.

Dear oil, cheap money

A second difference from previous oil shocks is that the impact on inflation has been surprisingly mild, thanks to the increased credibility of central banks as well as the downward pressure on prices exerted by competition from China and elsewhere. As a result, central banks have not needed to raise short-term rates sharply, so domestic demand, notably in America, has continued to grow more strongly than in the past and oil importers' current-account deficits remain large.

A third factor delaying the adjustment to external imbalances is that the oil producers are investing a large chunk of their windfall in global bond markets. In the 1970s and early 1980s, their surpluses were largely deposited in banks in America and Europe, which then lent the money to oil-importing developing countries (sowing the seeds of the 1981-82 Latin American debt crisis). This time, most of the money has gone into bonds, as well as equities, property and hedge funds.

A lot of it has ended up, via intermediaries in London, in America's bond market. This has reduced yields, supported American house prices and hence consumer spending, and so helped to sustain the country's external deficit. The IMF reckons that the oil exporters have shaved one-third of a percentage point off American bond yields.

America's deficit loomed large well before oil prices began their climb. But to the extent that

dearer energy has exacerbated that deficit, it has added to the risk of a sudden disorderly adjustment. It is commonly argued that because oil is traded in dollars, rising oil prices automatically increase the demand for greenbacks. But that is only a temporary effect. So far, the oil exporters seem happy to pile up their petrodollars in American Treasury bonds. But for how long? Speculation has grown over the past month that the Gulf states may decide to diversify their foreign assets, after American politicians forced Dubai's DP World to abandon its takeover of the running of six American ports. Debtors cannot afford to treat their creditors so rudely.

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Longevity

Eat less, live more

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How to live longer—maybe

DIETING, according to an old joke, may not actually make you live longer, but it sure feels that way. Nevertheless, evidence has been accumulating since the 1930s that calorie restriction—reducing an animal's energy intake below its energy expenditure—extends lifespan and delays the onset of age-related diseases in rats, dogs, fish and monkeys. Such results have inspired thousands of people to put up with constant hunger in the hope of living longer, healthier lives. They have also led to a search for drugs that mimic the effects of calorie restriction without the pain of going on an actual diet.

Amid the hype, it is easy to forget that no one has until now shown that calorie restriction works in humans. That omission, however, changed this month, with the publication of the initial results of the first systematic investigation into the matter. This study, known as CALERIE (Comprehensive Assessment of Long-term Effects of Reducing Intake of Energy), was sponsored by America's National Institutes of Health. It took 48 men and women aged between 25 and 50 and assigned them randomly to either a control group or a calorie-restriction regime. Those in the second group were required to cut their calorie intake for six months to 75% of that needed to maintain their weight.

The CALERIE study is a landmark in the history of the field, because its subjects were either of normal weight or only slightly overweight. Previous projects have used individuals who were clinically obese, thus confusing the unquestionable benefits to health of reducing obesity with the

possible advantages of calorie restriction to the otherwise healthy.

At a molecular level, CALERIE suggests these advantages are real. For example, those on restricted diets had lower insulin resistance (high resistance is a risk factor for type 2 diabetes) and lower levels of low-density lipoprotein cholesterol (high levels are a risk factor for heart disease). They showed drops in body temperature and blood-insulin levels—both phenomena that have been seen in long-lived, calorie-restricted animals. They also suffered less oxidative damage to their DNA.

Eric Ravussin, of Louisiana State University in Baton Rouge, who is one of the study's authors, says that such results provide support for the theory that calorie restriction produces a metabolic adaptation over and above that which would be expected from weight loss alone. (He also points out that it will be a long time before such work reveals whether calorie restriction actually extends life.) Nevertheless, such metabolic adaptation could be the reason why calorie restriction is associated with longer lifespans in other animals—and that is certainly the hope of those who, for the past 15 years, have been searching for ways of triggering that metabolic adaptation by means other than semi-starvation.

The search for a drug that will stave off old age is itself as old as the hills—as is the wishful thinking of the suckers who finance such efforts. Those who hope to find it by mimicking the effect of calorie restriction are not, however, complete snake-oil salesmen, for there is known to be a family of enzymes called sirtuins, which act both as sensors of nutrient availability and as regulators of metabolic rate. These might provide the necessary biochemical link between starving and living longer.

An elixir of life?

Boosting the activity of sirtuins in yeast, nematode worms and fruitflies (three rapidly reproducing stalwarts of biological laboratories) does indeed result in longer lifespans. In 2003 a team led by David Sinclair of Harvard Medical School described 19 plant-derived molecules that activate sirtuins in yeast. One of these molecules, resveratrol, is found in red wine—which created excitement among those who think that a wine-rich diet is part of the explanation for the healthy old age apparently enjoyed by many who live in southern Europe.

In February, a group led by Dario Valenzano of the Scuola Normale Superiore in Pisa, Italy, showed that the effect applies in vertebrates, too. Dr Valenzano's experiments with resveratrol increased the maximum lifespan of a small fish, called *Nothobranchius furzeri*, by 60%. (*Nothobranchius furzeri* was chosen because it is the shortest-lived vertebrate known, with a normal maximum lifespan of 12 weeks.)

Resveratrol, however, is only a starting point. Sirtris Pharmaceuticals, a firm based in Cambridge, Massachusetts, of which Dr Sinclair is a co-founder, has identified a number of synthetic molecules whose effect on yeast is many times more potent than resveratrol's. Although there is, as yet, no published evidence that sirtuins extend life in mammals, or that resveratrol activates sirtuins in human cells, some of these molecules are already in clinical trials for safety.

Moreover, Dr Sinclair thinks he knows why plant molecules such as resveratrol might affect longevity in animals. Resveratrol is produced when a vine is under stress—for example, due to dehydration or over-exposure to sunshine. According to Dr Sinclair's theory, which he calls xenohormesis, animals rely on such botanical stress signals to give them extra information about their own environments, in the same way that the alarm calls of one species warn others of danger. If bad things are happening to plants, he surmises, that is a reason for pre-emptive animal action. Animal bodies thus react to molecules such as resveratrol by activating their own

defence mechanisms. These, in turn, protect their cells from stress-related damage.

Xenohormesis is a variation of a more general theory, hormesis, which interests Suresh Rattan of Aarhus University in Denmark. A good example of hormesis is exercise. In theory, this should damage cells because it increases oxygen uptake, and oxidative stress is bad for things like DNA. Of course, exercise is not actually bad for cells—and the reason is that the body activates defence mechanisms which overcompensate for the stress the exercise creates, producing beneficial effects. So, while chronic stress is always bad for you, a short period of mild stress followed by a period of recovery can be good.

Many of the health benefits of exercise are thought to be due to the synthesis of damage-controlling molecules called heat-shock proteins, and Dr Rattan's group has been experimenting with other ways of triggering these proteins. He has found, for example, that taken in combination with exercise, a spice called curcumin boosts the production of heat-shock proteins several-fold.

According to Dr Rattan, such interventions improve the function of a cell over time, and in doing so, may produce clinical benefits such as protection against neurodegenerative diseases. Resveratrol may also produce benefits, he says, but how it does so is not yet clear. He disagrees with Dr Sinclair over the existence of a regulatory pathway for longevity in which sirtuins play a key role. In his view, ageing is about the accumulation of damage, and is not under tight genetic control. Sirtuins will, he says, probably be but a small part of a more complicated picture.

Dr Rattan also doubts whether calorie restriction will extend maximum human life expectancy. He argues that the concepts of ageing and longevity must be separated. It may, indeed, be possible to reduce or eliminate particular age-related diseases, and that would increase average lifespans in the way that eliminating other diseases has done in the past. But this is not the same as slowing down ageing itself, and thus increasing maximum lifespans. Longevity is a more complex trait than any individual disease, and, in his opinion, it will not be altered so easily.

Cynthia Kenyon, a researcher at the University of California, San Francisco, and a co-founder of Elixir Pharmaceuticals, another company looking into anti-ageing drugs, believes that molecules such as resveratrol are likely to be approved in the next five to ten years, for use as prophylactics against age-related diseases. People then will start taking them, and a huge natural experiment will get under way. If Dr Rattan is wrong, maximum lifespan as well as average lifespan will increase. If he is right, at least people will enjoy a healthier old age.

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Planetary science

White Mars

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Like Caesar's Gaul, the history of Mars is divided into three parts

WHETHER or not liquid water still exists on Mars, it is quite likely that it was there in the past. There is strong evidence of floods—and of channels carved by these floods—draining into the northern plains. There may have even been an ocean. Today, though, Mars appears as dry as a bone, and rarely gets warm enough to melt ice. So when, exactly, did it have water and for how long?

To tackle this question, Jean-Pierre Bibring, from the Institut d'Astrophysique Spatiale, in France, and his colleagues, looked at data gathered by an instrument on a spacecraft now orbiting Mars. *Mars Express* was built and launched by the European Space Agency (ESA) in 2003, and is the agency's first planetary mission—acquiring the moniker "express" because it was put together quickly and efficiently. It cost about €300m ($370m) to construct and dispatch.

ESA

A cheap shot

Using a spectrometer that maps Mars in visible and infra-red light, Dr Bibring's team has been able to create a detailed mineralogical map of most of the Martian surface, parts of which have just been published in *Science*. Through these minerals, says Dr Bibring, they can work out a geological history of the planet. What they find is not simply primeval volcanic rocks, but a rich array of secondary rocks that have been created by many processes. The geological history of Mars, it turns out, comes in three parts.

The earliest secondary minerals to form, says Dr Bibring, were clays. These need bodies of standing water to be around for long periods of time in order to come into existence. The only places on Mars where clays are detectable today are where the surface has been exposed to heavy erosion or a meteorite impact. This suggests clays formed early in Martian history, when water was available on the surface, and were then buried by other geological processes. Crucially, clays are found on the eroded flanks of riverbeds, but not on the beds themselves or the openings of channels. This suggests that the channels were eroded after the standing water had come and gone and the clays had already been formed.

Dr Bibring is uncertain about the precise dates of this first era. Mars is 4.5 billion years old, the same age as Earth. The clay-forming period, he surmises, began shortly after that—sometime between 4.4 billion and 4 billion years ago. If, during this period, large parts of Mars were covered with clays, the planet would have appeared white from space, not red.

The second step in Martian geological development started between 4 billion and 3.5 billion years ago, and was brief—lasting only a few hundred million years. This era began with a huge burst of volcanic activity that supplied a giant belch of sulphur-rich gases into the atmosphere, transforming the planet into a very acidic environment. At this time, water was not available for long enough to create clays, so none are found. But it must have been available transiently, because sulphate minerals, which also require water, were able to form.

The third, and final, era of Martian geology is the one that has lasted to this day. This is dominated by the oxidation of the surface to produce the ferric-oxide minerals that give the planet its red colour. Water did not play an important geological role in this era.

The significance of all this is that if one were to seek evidence of past life on Mars, then the best place to look would be in the clay-mineral deposits. First, they were formed during the conditions most favourable to life (at least, to life as it is known on Earth). Second, one of the theories of the origin of life on Earth suggests that clay minerals could be sites in which biochemical evolution takes place. Either way, these clay deposits could be a rich hunting ground for astrobiologists.

These results also add support to the idea that planetary science can be done relatively quickly and at modest cost—not least because last week another ESA planetary science spacecraft, *Venus Express*, arrived safely at its destination. What is particularly interesting about *Venus Express* is that it has reused the design of *Mars Express*, the same industrial teams, and even some spare parts left over from the earlier mission. It took three years to build and cost a miserly €220m.

That the Europeans are learning to recycle and reuse, whilst their American counterparts cannot manage such economies, should come as no surprise. ESA had a budget last year of €2.9 billion, about a fifth of NASA's. Necessity, as they say, is the mother of invention.

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Nuclear power

Nuclear fallout

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Arguments over the human impact of Chernobyl

Get article background

EPA

Sheltering from the storm

ON THE eve of the 20th anniversary of the nuclear disaster at the Chernobyl power station a row has broken out over its true human impact. A year ago a group calling itself the Chernobyl Forum said the accident would lead to far fewer deaths from cancer than had at first been predicted. The Chernobyl Forum comprises a number of United Nations agencies, including the International Atomic Energy Agency and the World Health Organisation, and also the governments of Belarus, Russia and Ukraine. The forum added that Chernobyl's real legacy was of a paralysing dread that had blighted the lives of those labelled “Chernobyl victims”.

However, Greenpeace, an environmental group, is challenging the forum's estimates that 9,300 people in the three countries concerned will die from cancer as a result of exposure to radiation from the plant. Blake Lee-Harwood, a spokesman for Greenpeace, said that their report looked at evidence from a wide range of sources and they believe that the death toll will be 100,000, an order of magnitude higher than the Chernobyl Forum estimate. However, this figure also includes deaths from causes other than cancer.

To complicate matters further, in the case of radiation damage time does not heal all wounds. For example, a commentary in this week's *Nature* by Dillwyn Williams of Strangeways Research Laboratory in Cambridge and Keith Baverstock at the University of Kuopio in Finland argues that lessons from the atomic bombings in Japan show that it can take far longer than 20 years for radiation-induced diseases to manifest themselves. The true cost of Chernobyl may not be known for decades.

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Cosmology and particle physics

What can the matter B?

Apr 20th 2006
From The Economist print edition

A new result bearing on the question of why the universe is made of matter

THAT people exist is more than a marvel explained by evolution. The presence of stars and planets vital to life—the very being of matter itself—is a wonder. For, at the moment at which the universe was created, matter and antimatter, being equal and opposite, should have been produced in equal and opposite amounts. Since, as every schoolboy knows, when matter and antimatter meet, they annihilate each other in a burst of energy, the equal amounts of matter and antimatter should have annihilated each other long ago and the universe should now be filled with energy and little else, which is evidently not the case. So what happened?

The key is that matter and antimatter are not, in fact, perfectly equal and opposite. In other words, they are not symmetrical—and that asymmetry favours matter. A few sources of asymmetry have already been found, but not enough to account for all the matter around. So physicists are eagerly seeking more, and two groups working at Fermilab, a particle-physics laboratory near Chicago, think they have found a candidate.

Their experiments involve a group of particles called B-mesons. Quantum mechanics allows B-mesons to turn into their antimatter counterparts and back again, a process known as mixing. This mixing is described by some deft but complicated mathematics, and is crucial to the question of asymmetry. The frequency at which it happens is related to a small but significant difference between the mass of the particle and its antiparticle.

The two experiments at Fermilab, each of which employed around 700 scientists from all over the world, have quantified the mixing process for a type of B-meson called B_s. The difference in mass between this particle and its antiparticle is greater than for other B-mesons studied to date, and so the frequency with which it oscillates is higher. The experiments found that B_s-mesons switch between being matter and antimatter some three trillion times a second.

Zippy though this undoubtedly is, it is slower than some predicted, ruling out some of the more exotic theories of particle physics. But the measurement does confirm there is more asymmetry around than had previously been detected. So, while it cannot fully explain the imbalance between matter and antimatter, it is a step in the right direction.

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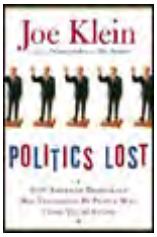
American politics 1

Dumb and dumber

Apr 20th 2006
From The Economist print edition

American politics today are micro-managed by an array of political professionals. A new book asks what exactly it is that they contribute

Politics Lost: How American Democracy Was Trivialised by People Who Think You're Stupid
By Joe Klein



Doubleday; 256 pages; $23.95

Buy it at
Amazon.com
Amazon.co.uk

ON THE evening that Martin Luther King was shot, Bobby Kennedy was due to speak in a black ghetto in Indianapolis. The audience had not yet heard the news and the police were worried about how they might react to being told by a white man. But Kennedy would not be deterred. “Ladies and gentlemen”, he began, “I'm only going to talk to you just for a minute or so this evening. Because I have some very sad news.”

The speech was one of the great pieces of political rhetoric: an oration that registered the enormity of the event while also beginning the work of healing. There were riots in 76 American cities over the next few days. Indianapolis remained quiet.

Kennedy's words marked the end of an era when politicians could dare to be natural. Today political professionals—consultants, pollsters and admen—test out every phrase. The result is a veritable Hobson's choice: the droning inanities of a John Kerry versus the scripted platitudes of a George Bush.

“Politics Lost”—the loss of all spontaneity in politics today—is everything that readers have come to expect from the author of “Primary Colours”. Based on a lifetime of careful observation, it is full of colourful vignettes and wonderful phrases (Michael Dukakis hailing from the “National Public Radio wing of the Democratic Party”), and it is suffused with powerful affection for the promise of American politics and exasperation at its reality.

Political consultants have taken the place of old-fashioned party bosses. They not only decide who gets what at every level of the political system; they embody their party's institutional memories. The most important relationship in politics is between two shadowy groups—the political aides who run the congressional campaign committees (those who dole out money to would-be candidates) and the political consultants (who dole out legitimacy). If you can't persuade the “right” consultant to work for you, you have little chance of getting on the political ladder.

These new lords of the political universe are a strange mix of eccentricity and cynicism. Dick Morris, the pompadoured pollster behind Bill Clinton's “triangulation” policy, was caught with a prostitute. Arthur Finkelstein, who did the most to make the word “liberal” radioactive, was a homosexual who eventually “married” his long-term partner. Both James Carville (who helped Mr Clinton) and the late Lee Atwater (George Bush senior) epitomised a certain Southern-fried weirdness.

Mr Klein convicts these consultants of an astonishing list of crimes—not just the generic vice of dumbing down democracy but also innumerable sins of incompetence. A hired-gun almost ruined Ronald Reagan's 1980 campaign before he was expelled by let-Reagan-be-Reagan loyalists. Susan Estrich took a bad candidate in Mr Dukakis and made him worse. Bob Shrum has lost all seven of the presidential campaigns he managed, notably steering Al Gore to disaster by persuading him to abandon Mr Clinton's winning formula in favour of a vacuous people-against-the-powerful populism. Yet this did not dissuade Mr Kerry from giving Mr Shrum another go.

So why do candidates hire consultants? One reason is that campaigns are such huge productions—arranged on a continental scale and often lasting more than 1,000 days. Even seat-of-the-pants candidates like John McCain in 2000 need specialists to arrange schedules and buy advertising. Another is that good consultants can work wonders. Remember how Atwater eviscerated Mr Dukakis? Or how Mr Carville, the “Ragin' Cajun”, choreographed the 1992 Clinton campaign.

The real issue is not whether you use consultants (everybody does) but how you manage them. Here the Republicans have been running rings around the Democrats for decades. The Republicans treat consultants as hired help rather than equal citizens. This means that they establish clear lines of authority and fire the duffers: there is no Republican Bob Shrum.

The real problem that Mr Klein is diagnosing is not the rise of the consulting industry. It is the loss of self-confidence of the political elite. And nowhere is this loss more desperately felt than in the party that gave us Bobby Kennedy.

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By Joe Klein.
Doubleday; 256 pages; $23.95

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American politics 2

Down and dirty

Apr 20th 2006
From The Economist print edition

WHEN Huey “Kingfish” Long was shot dead in his prime, millions of Americans believed their country had lost its political saviour. Millions more believed the assassinated populist possessed the worst characteristics of the Louisiana fish that inspired his nickname; characteristics summed up by a critic as “big mouth, feeds off suckers, thrives best in mud and slime, and is very hard to catch”.

Kingfish: The Reign of Huey P. Long
By Richard D. White

Random House; 384 pages; $26.95

Buy it at
Amazon.com
Amazon.co.uk

Richard White, a professor at Long's favourite university, Louisiana State, is not diverted by the fanciful conspiracy theories that continue to swirl around the politician's violent death in Baton Rouge in September 1935. He accepts the official story: Long was gunned down by Dr Carl Weiss, an ear-eye-nose-and-throat specialist whose family he had humiliated.

Long's biographer is interested instead in how his subject, after starting out as a salesman of laxatives and a highly alcoholic elixir for menstrual cramps, rose to be governor of the state of Louisiana, then a United States senator and finally the rival most feared by President Franklin Roosevelt. His verdict is even harsher than Robert Penn Warren's was in the literary classic that won a Pulitzer prize in 1947, “All the King's Men”.

Mr White concedes that Long was an inspiring orator and that he brought about some real improvements in the lives of many Louisianans. His state government increased school enrolment, taught illiterate adults to read, raised the state university to national stature and brought Louisiana out of the horse-and-buggy era by building lots of new roads and bridges. He nonetheless concludes that Long was always corrupt and cruel. What Kingfish said about sharing out the country's wealth to provide every American family with “enough for a home, an automobile, a radio, and the ordinary conveniences” was increasingly insincere. He proved it by, among other misdeeds, stealing public money, packing the state payroll with his friends and relatives, stuffing the ballot boxes and ruining his political rivals.

Long's spite was savage. He ordered the police to destroy the presses of a university newspaper that had the temerity to criticise him. He punished political rivals by publishing the names of their relatives in lunatic asylums. He resurrected and then circulated in a pamphlet an old rumour, lethal in the Cotton South, that a prominent local family had “coffee in its blood”.

In other states such outrageous behaviour would have discredited the governor. But, as Mr White explains, Louisiana was, and to a certain extent remains, different. America's political traditions had never gained a solid foothold in the state, where the illiteracy and poverty of many whites and the disenfranchisement of blacks deterred true democracy. Unlike states that began as British colonies with some representative government, democracy bypassed Louisiana under French and

Spanish rule. Just as plantation aristocrats and New Orleans politicos had done for generations, Long dominated the state—albeit more crudely.

Roosevelt had real cause to worry only when Long moved on from his state to the national stage as a potential candidate for the White House. The president foresaw a risk that a prolonged economic depression would cause people in America, much like those in Germany and Italy, to lose patience with democracy and turn to a radical demagogue like Long. Hard though it is to admit it, Kingfish's assassin may have done his country a good turn.

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President Hu in America

Feasting on the future

Apr 20th 2006
From The Economist print edition

WHEN did China cease to be a mysterious land and become something that affects us all? James Kynge dates the transition to early 2004, when iron manhole covers suddenly vanished from roads and pavements around the world. Chicago lost more than 150 in a month as thieves tried to satisfy China's thirst for scrap-metal; Scotland saw over 100 disappear in what was called the "great drain robbery". "In Montreal, Gloucester and Kuala Lumpur," writes Mr Kynge, "unsuspecting pedestrians stumbled into holes."

Both these books deal with China's economic ascent and its global implications—and both reach largely optimistic conclusions. Certainly more trade frictions lie ahead, nationalism is growing and there will possibly be a crisis over Taiwan, which the mainland is determined to ingest. But both books also argue that, by and large, China's rapid growth is sustainable; that its communist leaders will liberalise just enough to avoid serious social unrest and revolution; and that its foreign relations will be broadly peaceful. China's rise promises to be of continued benefit, both to its own people—with more than 400m lifted out of poverty since 1978—and to those on the outside who buy its cheap manufactured goods, provide it with energy, resources and know-how and profit from the low interest rates that are the result of its huge pool of savings.

In a particularly well-written book, Mr Kynge, a former China bureau chief of the *Financial Times*, brings alive all the complexities and contradictions of China's development. He traces its impact, travelling to Germany, Italy and America to talk to communities forced into painful but inevitable change as a result of China's rise. He also weaves in remarkable stories of Chinese entrepreneurs who disobeyed national edicts for a chance at a future, and who in the process are building modern China. One example is Yin Mingshan, who after 20 years in jail for "counter-revolutionary activities", went on to create a motorcycle company that in its heyday outsold Japan's Honda in parts of Asia.

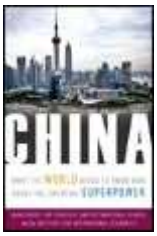
Mr Kynge combines a fresh perspective with an eye for arresting detail. A comparison of the rise of 19th-century Chicago with that of Chongqing today—which is growing eight times faster than the windy city—leads Mr Kynge to conclude that China's growth is "a compression of developmental time". He focuses on the effects of "malignant competition" that lead to profitless growth and a desperate lurch into overseas markets. Mr Yin complains that his motorcycles will soon sell for only a fraction above the scrap value of their metal. At Yiwu, the world's largest wholesale market,

China Shakes the World: The Rise of a Hungry Nation
By James Kynge

To be published in America by Houghton Mifflin in September
Weidenfeld & Nicolson; 244 pages; £18.99.

Buy it at
Amazon.com
Amazon.co.uk

China—The Balance Sheet: What the World Needs to Know Now About the Emerging Superpower
By the Centre for Strategic, International Studies and the Institute for International Economics



Public Affairs; 256 pages; $25 and £14.99

Buy it at

prices are a tenth of what they would be in the cheapest discount store in the West. One reason is blatant piracy. Mr Kynge spots four shops in a row sporting names like “Crocodile of the Yangtze” and “Croc Croc”, each one selling fake Lacoste goods. One shop assistant claims that “the French and the Chinese crocodile are the same brand. They have merged.”

Amazon.com
Amazon.co.uk

“China: The Balance Sheet”, a more academic read, is one of the most lucid and well-argued recent books on how the West should respond to China's rise. Published to coincide with President Hu Jintao's visit to Washington, it argues that America must continue to engage with China, however frustrating the process. The four authors, all experts on Asia, work for two leading Washington, DC, think-tanks and they make a convincing and balanced case. America is about $70 billion a year richer as a result of its trade with China, despite painful job losses in unskilled industries—and that figure will only grow. Thirty years from now, if current growth trends persist, China will be the world's largest economy. Meanwhile, China is also becoming Asia's foremost diplomatic and military power, even though its autocratic leadership is primarily focused on retaining domestic political control.

For all those reasons, America cannot shut China out but must draw it further into the global community. It should insist that the mainland start to play by international rules, by respecting intellectual property rights, reducing its trade barriers and revaluing its currency.

However, the book is also quite clear that the chief cause of America's difficulties is not China, but factors like technological change. To stay competitive, America must first put its own house in order by attending to its fiscal and trade deficits and strengthening its educational system to withstand an accelerated pace of globalisation. That way it will have little to fear—and much to gain—from China's ascent.

China Shakes the World: The Rise of a Hungry Nation.
By James Kynge.
Weidenfeld & Nicolson; 244 pages; £18.99.
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Deutsche Börse

Always look on the bright side

Apr 20th 2006
From The Economist print edition

WERNER SEIFERT, who until a year ago ran Deutsche Börse, the German exchange operator, was sacked by angry shareholders last May. He still does not seem to understand why, even though he has now written a book about the whole affair.

Mr Seifert's account, published only in German, demonises Christopher Hohn, a young hedge-fund manager, for playing the game of shareholder activism to the edge of legality—and winning. With only 8% of Deutsche Börse's shares, and a little help from like-minded investors, Mr Hohn scuppered Mr Seifert's bid for the London Stock Exchange, forcing a share buyback instead and some long overdue changes on Deutsche Börse's supervisory board.

Reuters

Piped sunshine

The rancour against hedge funds—the locusts (*Heuschrecken*) of the title—runs deep. Open capital markets are all very well, but taking shareholdings in rival stock exchanges and then ganging up to confound their attempts to merge is somehow unfair and should be made more difficult, he says. In an open letter to European finance ministers, Mr Seifert suggests how. But he fails to examine why not only Mr Hohn but also traditional investors such as Merrill Lynch Asset Management and Fidelity Investments became so exasperated with Deutsche Börse's poor governance.

In a prologue to this hugely one-sided account of the affair, Mr Seifert expresses the hope that others might learn from his mistakes. Yet he won't acknowledge Deutsche Börse's failure to give supervisory board power to its non-German shareholders—93% of the total—until it was too late, and even says that he would act no differently today. Mr Seifert's capacity for denial can be endearing, though. In the lift on the way to his “execution”, he recalls humming an appropriate ditty from Monty Python's “Life of Brian”: “Always look on the bright side of life.”

Invasion der Heuschrecken: Intrigen, Machtkämpfe, Marktmanipulation.
By Werner G. Seifert with Hans-Joachim Voth.
Econ; 272 pages; €19.95

Invasion der Heuschrecken: Intrigen, Machtkämpfe, Marktmanipulation
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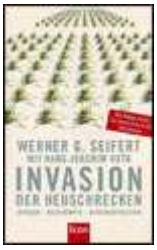

Econ; 272 pages; €19.95

Buy it at
Amazon.de

The Royal Academy

School for scandal

Apr 20th 2006
From The Economist print edition

WHAT fun to be a fly on the wall when the Royal Academicians—architects as well as painters—discuss James Fenton's history of their antique organisation. Mr Fenton, who is a great all-rounder—poet, critic, lyricist and tropical fruit farmer—was commissioned by the Royal Academy (RA) to give them “an outsider's unofficial view”. Mr Fenton has written an occasionally compelling and rather peculiar book—not least because his version of the RA's history mocks the book's title.

The RA has been a great survivor, exhibiting new British art each summer, filling its fine rooms with shows of great masters, and running an art school. Only rarely has it been a school of genius. Often it has been quite the reverse.

During its 238-year existence, genius flourished only in the early decades. J.M.W. Turner stands out, as does John Constable, though his election was delayed until he was 52 because Sir Thomas Lawrence, the president at the time, did not approve of his work. Even Sir Joshua Reynolds, the RA's distinguished first president, felt so insulted by his fellows that he resigned from the post—and the RA—until King George III persuaded him to change his mind. There was no place for William Blake.

School of Genius: A History of the Royal Academy of Arts
By James Fenton

Royal Academy of Arts; 319 pages; £35. To be published in America by the Royal Academy in June

Buy it at
Amazon.com
Amazon.co.uk

In the last 100 years, the RA has rejected, or been rejected by, a whole hall of fame of British painting, including Henry Moore, Barbara Hepworth, Ben Nicholson, Graham Sutherland, John Piper, Francis Bacon, Howard Hodgkin, Richard Hamilton, and Frank Auerbach. Among artists and their audience, the reputation of the RA reached its nadir during the presidency of Sir Alfred Munnings, who took office in 1944; “a truly disastrous presidency”, says Mr Fenton.

Munnings was famous for denigrating modern painters, Picasso especially, but he was worse than a malign critic. He actually tried to persuade policemen to bring a prosecution against Sir Stanley Spencer, a fellow academician, under Britain's obscenity laws. Philistinism reigned. Sir William Llewellyn, president from 1928-1938, claimed that the RA's hanging committee for the summer exhibition would have rejected Giorgione's “La Tempesta”. Sir Gerald Kelly, who followed Munnings, declared that Cézanne was “a giant who didn't come off”. When Jacob Epstein's nude figures were removed from an office building in the Strand in 1935, the RA said not a word.

Mr Fenton is even more displeased by the RA's decision to sell a Leonardo da Vinci cartoon in 1962—it is now one of the National Gallery's treasures—and by the disposal of other important drawings from its excellent collection. The rationalisation at the time was that the academy's independence needed to be preserved. Mr Fenton has little time for that argument, pointing out that no organisation that pays the government a peppercorn rent of £1 for 999 years for its

elegant quarters in Burlington House can be described as independent.

The RA's reputation between 1966 and 1984 revived during the presidencies of Sir Thomas Monnington and Sir Hugh Casson—all presidents are routinely knighted. But serenity escapes it. Recently, Lawton Fitt, an American businesswoman, resigned as the RA's secretary after a bout of vicious office politics, while another official, entitled the keeper of the RA schools, was unceremoniously chucked out of the academy in a dispute about the use of funds.

Mr Fenton, whose fluent narrative is interrupted by entertaining digressions into the idea of an academy, eccentric painters and dedicated artists' models, does finally ask the obvious question: What is the RA for? But his answer is less robust than his history. “Artists need representation, and although the meaning of such a sentence may change, the statement remains true.” Is that all? Is it enough?

School of Genius: A History of the Royal Academy of Arts.
By James Fenton.
Royal Academy of Arts; 319 pages; £35. To be published in America by the Royal Academy in June

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Early music

Savall the saviour

Apr 20th 2006 | NEW YORK
From The Economist print edition

The viola da gamba is enjoying a new lease of life, thanks to a Catalan enthusiast

"ALL the essential things between a man and a woman are said softly. Music is the same." Or so says Jordi Savall, a courtly 64-year-old Catalan whose lifelong study of the viola da gamba has led to the rehabilitation of an eloquent instrument that has been neglected for more than 200 years.

Dating back to the 15th century, the viol looks something like a lightly-built cello. But its sound could hardly be more different. It has seven strings, which are richly resonant though less tense than the cello's four. This gives a softer, earthier sound that is completely unsuited to large concert halls and big orchestras, and which undoubtedly contributed to its decline during the Baroque period. Mr Savall studied the cello as a boy and became interested in the viola da gamba only when he began playing with an early music group. Even so, there was little tradition to follow and hardly any music to play.

Lebrecht Collection

Bowing to the bow

What might have stumped a less dedicated musician only proved a challenge for Mr Savall. Following the example of another Catalan native, Pablo Casals, whose groundbreaking interpretation of Bach's cello suites followed a rigorous 12-year-study of the pieces in the late 19th century, Mr Savall began seeking out forgotten viol music to resurrect, practising ten hours a day for a decade before recording any of the neglected viol repertoire.

"To find an unknown score was very exciting," he says. "Most of my friends preferred to play things they knew." One composer Mr Savall researched was Marin Marais, a favourite of Louis XIV's, whose detailed musical scores were filled with annotations of every nuance of viol-playing from bowing to dynamics.

Mr Savall's study of Marais inspired his robust, soulful performances on the soundtrack of "Tous les Matins du Monde". Alain Corneau's elegant 1991 French film about Marais and his teacher, Monsieur de Sainte Colombe, also helped to cement the commercial viability of early music. The 53 discs on the Alia Vox label have sold more than 1m copies since Mr Savall founded it in 1998.

In addition to rediscovering lost scores, Mr Savall set about completely reinventing a playing technique that would help him draw the best from the delicate instrument. Today, he is as popular a teacher as he is a player.

During a recent master-class at the Metropolitan Museum in New York last month, he urged his students to try and understand the basic language of their instrument. “You must play with the bow on air,” he explained, meaning that to draw music from the strings the bow must be lifted to allow the sound to drift. A quick demonstration of what he meant produced immediate and startling results as Mr Savall replaced his students' dull, muted sound with gracefully seductive singing lines.

Unlike the moody and reclusive Sainte Colombe of the film, Mr Savall is a patient guide. His heavily accented English is woven with anecdotes in French, one of the seven languages he speaks fluently. He asked a student at the masterclass to sing, as “music starts before playing. Only if you can sing inside and out can you transmit the song.”

The masterclass seemed surprised to hear they should perform with the score. But for Mr Savall memorisation is the same as playing on autopilot, and stifles a necessary element of unpredictability. “The only contact we have with the composer is the music,” he explains. “It is important to have this relationship, but it's a balance between discipline and freedom.” The vital art of improvisation encourages this freedom, and Mr Savall urges players of early music to exploit it in full to help keep the repertoire alive.

In this, Mr Savall was inspired by the writings of Diego Ortiz, a 16th-century composer who detailed the rules of improvisation. Like jazz players, early musicians can embellish melodies and chords within a certain structure. Mr Savall improvises along with his soprano wife, Montserrat Figueras, and their two children, who play the harp and the lute in Hespèrion XXI, one of at least three ensembles he has formed and with which he now tours the world.

“Hespèrion” derives from the ancient Greek word “Hesperia,” meaning west, and refers to the Iberian peninsula. Hespèrion XXI has revived many obscure composers, making a profound contribution to Spanish music. Mr Savall says his curiosity to discover ancient music is insatiable, as is his gift to share and to reinvent. As he told one student at the masterclass: “playing viol has to be like explaining something. People will listen if you tell it in an interesting way.”

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Muriel Spark

Apr 20th 2006
From The Economist print edition

Getty Images

Dame Muriel Spark, novelist, died on April 13th, aged 88

AS SHE lay on the divan in her flat in Queen's Gate, Caroline Rose suddenly heard the sound of a typewriter. Tap-tappity-tap.

> It seemed to come through the wall on her left. It stopped, and was immediately followed by a voice remarking her own thoughts. It said: On the whole she did not think there would be any difficulty with Helena.

Caroline, on another plane of existence, was Muriel Spark. She was trying to scrape a living by writing in London in the mid-1950s, divorced, with a small son. Coffee and diet pills kept her going, but also gave her hallucinations. Because “if you're going to do a thing, you should do it thoroughly”, she had converted in 1954 from vague Christianity to Roman Catholicism. In her first published novel, “The Comforters” (1957), she was both Caroline and God, or fate, or that ubiquitous typewriter, tapping out behind the wall page after page of Caroline's life.

God loomed large in Ms Spark's dark, biting, witty novels. In the early years of her career it was the vogue for Catholic converts to be obsessed with Him, sin, and themselves. But unlike Evelyn Waugh, who warmly praised her, or Graham Greene, who kept her going with a monthly allowance and cases of wine, Ms Spark preferred to leave aside the heavier, guilt-ridden aspects of the faith. Her newly-made Catholics were comic and somewhat tentative. They did not agonise much. But, like her, they were perplexed that a divine Creator should allow evil in the world, and especially intrigued by the permutations of free will and fate.

Fate had taken Ms Spark to Africa in 1937, to a miserable marriage from which she escaped six years later. But Africa also gave her the material for a short story, “The Seraph and the Zambesi”, with which she won the *Observer*'s Christmas short story competition in 1951. After this,

gradually, she became famous. She wrote 23 novels, mostly daring, usually surprising and impossible, as she proudly said, to classify. Anything, it seemed, might inspire a burst of that needle-sharp pen, from Watergate (“The Abbess of Crewe”, 1974) to the disappearance of Lord Lucan (“Aiding and Abetting”, 2000). Her works were short, tight and beautifully constructed, hinting perhaps at the poet she would slightly have preferred to be.

Dabblings on the dark side held a particular fascination. “The Ballad of Peckham Rye” (1960) satirised Satanism in south London, while “The Bachelors” (1960) anatomised spiritualism in Victoria. (“The Interior Spiral...That's a make of mattress, isn't it?”) Her light touch still managed to carry maximum disapproval. A phrase, too, could pin down more or less anything she spotted. “The evening paper rattle-snaked its way through the letter box and there was suddenly a six-o'clock feeling in the house.” “She yawned with her mouth all over her face.” Bathos was a speciality: “Human nature is apt to fail in spite of regular prayer and deep breathing”.

The beginning and the end

By birth and childhood formation Ms Spark was a Scottish writer, and always acknowledged it. Like freckles, as she said, her Scottishness could never be lost, though in her later Italian exile she revelled at being European. She wrote of Edinburgh with a child's intensity: the “amazingly terrible” smells of the Old Town, the sight of the unemployed fighting, spitting and cursing, but also the way it might become “a floating city when the light was a special pearly white”.

Her own neighbourhood, Bruntsfield, was middle-class, and her parents Jewish-Episcopalian. But she became gradually aware of the Calvinism around her, symbolised by the frightening blackened stone of the city's churches. The God of Calvin, as she wrote in “The Prime of Miss Jean Brodie”, her small autobiographical masterpiece of Edinburgh public-school life, “sees the beginning and the end”.

As a writer, she could see it too. In “Brodie”, which became both a play and a film, she ran dizzyingly forwards and backwards in time, revealing how her characters would turn out or how they would die. There was, it seemed, quite a streak of Ms Spark in the scatty, romantic Miss Brodie: “Safety does not come first. Goodness, Truth and Beauty come first.” But Ms Spark painted herself as Sandy Stranger, a clever, ugly girl with “small, almost non-existent” eyes. Sandy was the sly onlooker and chief teller of the tale, as well as the puller of the strings. It was she, naturally, who betrayed Miss Brodie to the authorities and ended her teaching career. And Sandy, after one torrid affair and one acclaimed book on psychology, became an enclosed nun, Sister Helena of the Transfiguration.

Nunnishness, it might be thought, figured little in Ms Spark's real life. Instead there was fame, many prizes (though she missed out on the Booker, the biggest British fiction award), sleek clothes, and a fortune that drove her abroad to escape the taxman. Yet she lived for 27 years in a converted 13th-century church in Tuscany, happily eschewing the literary whirl, writing longhand in spiral-bound notebooks that were sent to her from Edinburgh. And she died in the Easter season, the best time for Catholics, in a way that might almost have been planned. Tap-tappity-tap.

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Overview

Apr 20th 2006
From The Economist print edition

The **oil price** broke records, thanks to some diplomatic blustering in Iran and falling petrol stocks in America. A barrel of West Texas Intermediate, a benchmark crude, rose above $72.00 during trading this week.

Higher energy prices helped boost American **inflation**. Consumer prices rose by 0.4% in March, leaving them 3.4% higher than a year earlier. Core prices, excluding energy and food, rose by 0.3%, the biggest monthly gain in more than four years, leaving them 2.1% higher than a year ago. Further up the production chain, wholesale prices rose by 3.5% in the year to March.

Unless these figures spook America's central bankers, their next **interest-rate rise** is likely to be their last, judging by the minutes of the Federal Reserve's March meeting, released this week. “Most members thought that the end of the tightening process was likely to be near,” the minutes said, “and some expressed concerns about the dangers of tightening too much.”

America's **trade deficit** in goods and services narrowed to $65.7 billion in February, $2.8 billion less than the record deficit set in January. America attracted a surprisingly strong **inflow of foreign capital** in February. Net foreign purchases of securities amounted to $86.9 billion, compared with $69.1 billion the month before. Private investors bought a net $10.8 billion-worth of Treasury bonds and notes, having been net sellers the month before; demand for bonds issued by government agencies was also brisk.

America's **industrial production** rose by 0.6% in March, leaving it 3.6% above its level of a year earlier. American industry is now operating at 81.3% of full capacity, just above its long-run average. But **house-building** is slowing. Construction began on 1.96m new houses in March—at a seasonally adjusted, annualised rate—a slower pace of building than in any month since March 2005.

Japan's producer prices are still rising at a healthy pace. The price index for corporate goods rose by 2.7% in the year to March.

In Britain the **unemployment** rate edged up to 5.1%, or 1.56m people, in the three months to February, compared with 4.8% a year earlier. Average earnings, including bonuses, rose by 4.2% in the three months to February.

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Output, demand and jobs

Apr 20th 2006
From The Economist print edition

% change on year ago

	GDP		The Economist poll GDP forecasts		Industrial production		Retail sales (volume)		Unemployment % rate		
	latest	qtr*	2006	2007	latest		latest		latest		year ago
Australia	+ 2.7	Q4 + 1.9	+ 3.1	+ 3.4	+ 0.6	Q4	+ 1.9	Q4	5.0	Mar	5.2
Austria	+ 2.1	Q4 + 2.8	+ 2.2	+ 1.9	+ 8.2	Jan	+ 4.5	Jan	5.0	Mar	5.1
Belgium	+ 1.5	Q4 + 2.6	+ 2.2	+ 1.8	+ 6.3	Feb	– 2.5	Jan	12.4	Feb†	12.7
Britain	+ 1.8	Q4 + 2.3	+ 2.3	+ 2.4	– 1.4	Feb	+ 2.1	Feb	5.1	Feb‡	4.8
Canada	+ 2.9	Q4 + 2.5	+ 3.1	+ 2.8	+ 0.9	Jan	+ 4.4	Jan	6.3	Mar	6.9
Denmark	+ 3.3	Q4 – 0.1	+ 2.8	+ 2.2	+ 7.1	Feb	+ 3.8	Feb	5.0	Feb	6.0
France	+ 1.5	Q4 + 1.4	+ 2.0	+ 2.0	– 0.3	Feb	+ 1.7	Feb	9.6	Feb	10.1
Germany	+ 1.0	Q4 nil	+ 1.8	+ 1.2	+ 3.2	Jan	+ 1.1	Feb	11.4	Mar§	12.1
Italy	+ 0.5	Q4 + 0.1	+ 1.2	+ 1.1	+ 3.4	Feb	+ 0.2	Jan	7.7	Dec	7.9
Japan	+ 4.0	Q4 + 5.4	+ 3.0	+ 2.4	+ 3.7	Feb	– 0.2	Feb	4.1	Feb	4.6
Netherlands	+ 1.6	Q4 + 3.2	+ 2.5	+ 1.9	+ 0.6	Feb	+ 7.4	Jan	5.9	Mar††	6.7
Spain	+ 3.5	Q4 + 3.9	+ 3.1	+ 2.7	+ 2.3	Feb	+ 0.1	Feb	8.7	Feb	9.9
Sweden	+ 2.9	Q4 + 2.6	+ 3.3	+ 2.8	+ 1.5	Feb	+ 7.7	Feb	5.6	Feb†	5.7
Switzerland	+ 2.7	Q4 + 2.1	+ 2.3	+ 1.7	+ 3.9	Q4	+ 0.4	Feb	3.6	Mar†	3.9
United States	+ 3.2	Q4 + 1.7	+ 3.3	+ 2.8	+ 3.6	Mar	+ 5.1	Feb	4.7	Mar	5.1
Euro area	+ 1.7	Q4 + 1.0	+ 2.1	+ 1.7	+ 2.5	Jan	+ 1.0	Feb	8.2	Feb	8.8
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*										
Finland	+ 2.9	Q4 + 3.7	na	na	+ 3.5	Feb	+ 5.8	Jan	8.1	Feb	9.0
Greece	+ 3.7	Q4 na	na	na	– 1.7	Feb	+ 0.5	Jan	9.7	Q4	10.4
Iceland	+ 3.6	Q4 na	na	na	na		na		1.6	Feb†	2.8
Ireland	+ 5.7	Q4 + 7.6	na	na	– 5.2	Feb	+ 6.0	Feb	4.5	Mar	4.4
Luxembourg	+ 3.1	Q1‡‡ na	na	na	+12.7	Jan	+ 9.1	Feb	4.7	Feb	4.4
New Zealand	+ 1.9	Q4 nil	na	na	– 2.9	Q4	+ 3.0	Q4	3.6	Q4	3.6
Norway	+ 2.5	Q4 + 1.0	na	na	+ 0.5	Feb	+ 2.8	Feb	4.2	Jan**	4.5
Portugal	+ 0.7	Q4 + 0.4	na	na	– 1.5	Feb	+ 3.0	Feb	8.0	Q4†	7.1

*% change on previous quarter at an annual rate. †Not seasonally adjusted. ‡Dec-Feb; claimant count rate 3.0% in Mar.
§EU harmonised rate 8.9% in Feb. ††Jan-Mar. ‡‡2005. **Nov-Jan.

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Prices and wages

Apr 20th 2006
From The Economist print edition

% change on year ago

	Consumer prices			The Economist poll consumer prices forecast		Producer prices			Wages/earnings		
	latest		year ago	2006	2007	latest		year ago	latest		year ago
Australia	+ 2.8	Q4	+ 2.6	+ 2.8	+ 2.7	+ 4.8	Q4	+ 8.2	+ 5.3	Q4	+ 2.9
Austria	+ 1.2	Feb	+ 3.2	+ 1.9	+ 1.8	+ 1.9	Mar	+ 4.0	+ 2.7	Mar	+ 2.2
Belgium	+ 1.7	Mar	+ 3.1	+ 2.1	+ 1.8	+ 3.7	Feb	+ 4.3	+ 2.3	Oct	+ 2.4
Britain	+ 2.0	Feb*	+ 1.6	+ 2.0	+ 1.9	+ 2.5	Mar	+ 2.9	+ 4.2	Feb†	+ 4.6
Canada	+ 2.2	Feb	+ 2.1	+ 2.1	+ 2.1	+ 0.6	Feb	+ 2.8	+ 0.6	Jan	+ 2.0
Denmark	+ 1.9	Mar	+ 1.4	+ 1.9	+ 2.0	+ 3.8	Mar	+ 4.2	+ 2.9	Q4	+ 2.9
France	+ 1.5	Mar	+ 1.9	+ 1.7	+ 1.5	+ 3.5	Feb	+ 3.1	+ 3.3	Q4	+ 3.0
Germany	+ 1.8	Mar	+ 1.8	+ 1.6	+ 2.3	+ 2.5	Mar	+ 3.3	+ 1.1	Jan	+ 1.1
Italy	+ 2.1	Mar	+ 1.9	+ 2.1	+ 1.9	+ 4.9	Feb	+ 4.7	+ 2.6	Feb	+ 3.4
Japan	+ 0.5	Feb	– 0.3	+ 0.4	+ 0.6	+ 2.7	Mar	+ 1.4	+ 0.4	Feb	+ 0.1
Netherlands	+ 1.0	Mar	+ 1.8	+ 1.6	+ 1.5	+ 5.6	Feb	+ 5.2	+ 1.7	Mar	+ 0.6
Spain	+ 3.9	Mar	+ 3.4	+ 3.5	+ 2.8	+ 6.3	Feb	+ 4.9	+ 2.5	Q4	+ 2.7
Sweden	+ 1.1	Mar	+ 0.1	+ 1.2	+ 1.8	+ 4.9	Feb	+ 2.8	+ 3.4	Dec	+ 2.0
Switzerland	+ 1.0	Mar	+ 1.4	+ 1.2	+ 1.2	+ 1.6	Mar	+ 1.4	+ 0.9	2004	+ 1.4
United States	+ 3.4	Mar	+ 3.0	+ 3.0	+ 2.3	+ 3.5	Mar	+ 4.9	+ 3.4	Mar	+ 2.6
Euro area	+ 2.2	Mar	+ 2.1	+ 2.0	+ 2.0	+ 5.4	Feb	+ 4.2	+ 2.4	Q4	+ 2.4
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*										
Finland	+ 0.9	Mar	+ 1.0	na	na	+ 5.3	Mar	+ 2.4	+ 3.5	Q4	+ 4.3
Greece	+ 3.3	Mar	+ 2.9	na	na	+ 8.9	Feb	+ 4.1	na		na
Iceland	+ 4.5	Apr	+ 4.3	na	na	+ 4.2	Mar	+ 7.0	+ 8.6	Feb	+ 6.7
Ireland	+ 3.5	Mar	+ 2.1	na	na	+ 3.3	Feb	– 0.4	+ 3.8	Q4	+ 4.6
Luxembourg	+ 3.0	Mar	+ 2.4	na	na	+ 3.9	Feb	+17.7	+ 2.5	Jan	+ 0.2
New Zealand	+ 3.4	Q1	+ 2.8	na	na	+ 6.5	Q4	+ 3.4	+ 3.1	Q4	+ 2.5
Norway	+ 2.4	Mar	+ 1.0	na	na	+15.1	Mar	+17.5	+ 3.1	Q4	+ 3.9
Portugal	+ 3.1	Mar	+ 2.2	na	na	+ 5.9	Feb	+ 4.0	nil	Feb	– 1.5

*RPI inflation rate 2.4% in Feb. †Dec-Feb.

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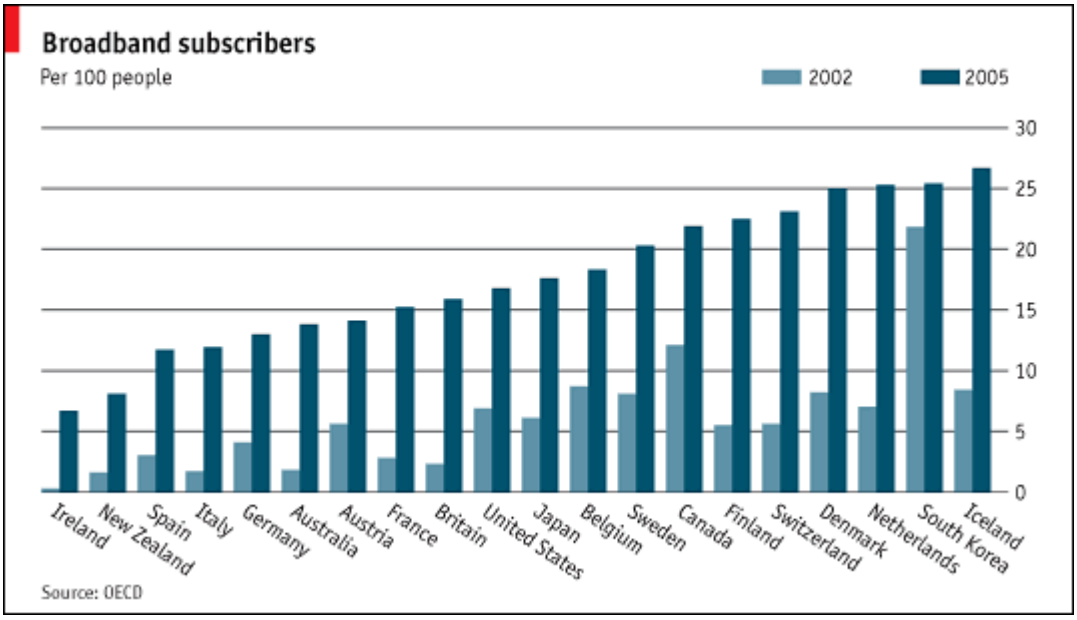
Broadband subscribers

Apr 20th 2006
From The Economist print edition



At the end of last year OECD countries had 158m broadband subscribers, equivalent to 13.6 subscribers for every 100 people—up from 4.9 in 2002. Iceland has the highest penetration rate, at 27%. South Korea, the Netherlands and Denmark also have rates of more than 25%. A more modest 17% of Americans have broadband. At the other extreme, Ireland and New Zealand have rates of less than 10%.

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Money and interest rates

Apr 20th 2006
From The Economist print edition

	Money supply* % change on year ago			Interest rates % p.a. (Apr 19th 2006)					
				3-mth money market		2-year	10-year gov't bonds		corporate
	narrow	broad		latest	year ago	gov't bonds	latest	year ago	bonds
Australia	+ 6.7	+ 7.5	Feb	5.67	5.72	5.54	5.58	5.34	6.62
Britain	+ 6.2	+12.2	Feb	4.58	4.88	4.45	4.44	4.58	5.12
Canada	+10.0	+ 6.4	Feb	3.96	2.44	4.13	4.40	4.19	5.56
Denmark	+20.2	+14.4	Feb	2.85	2.18	3.26	3.91	3.49	5.22
Japan	+ 5.0	+ 1.5	Mar	0.04	0.02	0.67	1.87	1.25	2.03
Sweden	+ 1.3	+ 8.8	Feb	2.04	1.97	2.95	3.75	3.51	3.67
Switzerland	+ 1.6	+ 4.7	Mar	1.28	0.76	1.68	2.55	2.06	2.61
United States	+ 0.8	+ 4.7	Mar‡	4.83	3.05	4.87	4.93	4.21	5.97
Euro area†	+ 9.9	+ 8.0	Feb	2.77	2.14	3.26	3.83	3.42	4.42

*Narrow: M1 except Britain and Sweden M0, broad: M2 or M3 except Britain M4. † Germany for bonds. ‡ New series for broad money supply. Benchmarks: US 30-year 4.84%, Japan No. 278 1.88%. Central bank rates: US fed funds 4.75%, ECB refinancing 2.50%, BOJ overnight call 0.001%, BOE repo 4.5%. Sources: Bank of Canada, Commerzbank, Danske Bank, Global Insight, JPMorgan Chase, Stockholmsbörsen, UBS, Westpac, Thomson Datastream. Rates cannot be construed as banks' offers.

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Stockmarkets

Apr 20th 2006
From The Economist print edition

Market indices

	Apr 19th	2006 high	2006 low	% change on one week	% change on record high	% change on Dec 30th 2005 in local currency	% change on Dec 30th 2005 in $ terms
Australia (All Ordinaries)	5,233.1	5,233.1	4,708.8	+ 1.8	nil	+11.1	+12.9
Austria (ATX)	4,226.9	4,226.9	3,682.4	+ 2.8	nil	+15.3	+20.5
Belgium (Bel 20)	3,861.8	3,978.0	3,573.9	+ 0.6	- 2.9	+ 8.8	+13.8
Britain (FTSE 100)	6,089.8	6,089.8	5,618.8	+ 1.5	-12.1	+ 8.4	+12.9
Canada (Toronto Composite)	12,487.3	12,487.3	11,272.3	+ 2.6	nil	+10.8	+13.7
Denmark (OMXCB)	370.7	395.5	362.0	+ 0.1	- 6.3	+ 0.8	+ 5.3
France (SBF 250)	3,647.3	3,709.4	3,327.6	+ 1.3	-16.9	+10.5	+15.5
(CAC 40)	5,158.1	5,255.3	4,748.3	+ 1.4	-25.5	+ 9.4	+14.4
Germany (DAX)*	5,993.8	6,031.4	5,334.3	+ 1.6	-25.7	+10.8	+15.9
Italy (S&P/MIB)	38,047.0	38,602.0	35,652.0	+ 0.8	-24.1	+ 6.6	+11.4
Japan (Nikkei 225)	17,350.1	17,563.4	15,341.2	+ 1.1	-55.4	+ 7.7	+ 7.9
(Topix)	1,747.3	1,783.7	1,572.1	+ 0.3	-39.4	+ 5.9	+ 6.1
Netherlands (AEX)	468.9	472.6	431.5	+ 1.1	-33.2	+ 7.3	+12.2
Spain (Madrid SE)	1,275.3	1,296.0	1,156.8	+ 1.0	- 1.6	+10.3	+15.3
Sweden (Affarsvarlden Gen)	331.5	333.6	287.3	+ 1.4	-17.2	+13.0	+19.3
Switzerland (Swiss Market)	8,050.9	8,109.3	7,583.9	+ 0.9	- 4.3	+ 6.2	+10.1
United States (DJIA)	11,278.8	11,317.4	10,667.4	+ 1.3	- 3.8	+ 5.2	+ 5.2
(S&P 500)	1,309.9	1,311.6	1,248.3	+ 1.7	-14.2	+ 4.9	+ 4.9
(NASDAQ Comp)	2,370.9	2,370.9	2,205.3	+ 2.4	-53.0	+ 7.5	+ 7.5
Europe (FTSEurofirst 300)†	1,384.0	1,384.0	1,277.1	+ 1.4	-18.8	+ 8.5	+13.4
Euro area (FTSE Euro 100)†	1,176.3	1,193.1	1,078.9	+ 1.1	-24.1	+ 8.0	+12.9
World (MSCI)‡	1,363.4	1,363.4	1,259.1	+ 2.2	- 5.9	+ 8.4	+ 8.4
World bond market (Citigroup)††	620.5	638.9	612.1	+ 0.9	- 2.9	nil	nil

*Total return index. †In euro terms. ‡Morgan Stanley Capital International index includes individual markets listed above plus eight others, in $ terms. ††Citigroup World Government Bond Index, total return, in $ terms.

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Trade, exchange rates and budgets

Apr 20th 2006
From The Economist print edition

	Trade balance*, $bn latest 12 months		Current-account balance $bn latest 12 mths		The Economist poll % of GDP, forecast 2006	2007	Exchange rate trade-weighted† 2000=100 Apr 19th	year ago	Currency units per $ Apr 19th	year ago	per £	per euro	per ¥100	Budget balance % of GDP 2005‡
Australia	− 12.8	Feb	− 42.1	Q4	− 5.5	− 5.0	117.9	115.3	1.34	1.29	2.40	1.65	1.14	+ 1.0
Austria	− 1.9	Jan	+ 0.5	Dec	+ 0.1	+ 0.1	104.8§	105.8	0.81	0.77	1.45	–	0.69	− 2.0
Belgium	+ 12.3	Feb	+ 6.6	Dec	+ 2.0	+ 2.1	106.4§	107.7	0.81	0.77	1.45	–	0.69	nil
Britain	−121.5	Feb	− 57.4	Q4	− 2.5	− 2.5	98.4	101.6	0.56	0.52	–	0.69	0.47	− 3.1
Canada	+ 59.9	Feb	+ 25.2	Q4	+ 2.2	+ 1.6	127.3	115.3	1.14	1.24	2.04	1.40	0.97	+ 1.3
Denmark	+ 8.7	Feb	+ 6.0	Feb	+ 2.7	+ 2.5	106.2	106.5	6.05	5.70	10.8	7.46	5.13	+ 2.8
France	− 30.3	Feb	− 43.5	Feb	− 1.6	− 1.3	107.1§	108.6	0.81	0.77	1.45	–	0.69	− 3.2
Germany	+195.8	Feb	+113.3	Feb	+ 3.9	+ 4.1	108.5§	110.2	0.81	0.77	1.45	–	0.69	− 3.9
Italy	− 16.3	Feb	− 26.5	Jan	− 1.5	− 1.4	106.7§	108.1	0.81	0.77	1.45	–	0.69	− 4.3
Japan	+ 86.5	Feb	+163.4	Feb	+ 3.7	+ 3.6	80.7	86.9	118	107	211	145	–	− 6.5
Netherlands	+ 39.1	Feb	+ 39.8	Q4	+ 5.7	+ 5.6	107.2§	108.5	0.81	0.77	1.45	–	0.69	− 1.6
Spain	− 97.6	Jan	− 82.3	Jan	− 7.3	− 7.4	105.1§	106.0	0.81	0.77	1.45	–	0.69	+ 0.3
Sweden	+ 19.2	Feb	+ 21.8	Q4	+ 6.5	+ 6.1	97.0	98.9	7.54	7.03	13.5	9.30	6.40	+ 1.2
Switzerland	+ 7.0	Feb	+ 50.2	Q4	+13.0	+12.3	106.0	108.0	1.27	1.18	2.27	1.57	1.08	− 1.6
United States	−798.3	Feb	−804.9	Q4	− 6.8	− 6.7	85.5	82.6	–	–	1.79	1.23	0.85	− 3.7
Euro area	+ 18.1	Jan	− 40.3	Jan	− 0.3	− 0.1	117.8	118.6	0.81	0.77	1.45	–	0.69	− 2.9
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*													
Finland	+ 9.5	Feb	+ 4.2	Feb	na	na	107.9§	109.2	0.81	0.77	1.45	–	0.69	+ 2.1
Greece	− 34.5	Jan	− 18.1	Jan	na	na	104.1§	104.9	0.81	0.77	1.45	–	0.69	− 4.5
Iceland	− 1.6	Feb	− 2.6	Q4	na	na	106.2**	98.2	78.5	62.5	140	96.8	66.6	+ 2.0
Ireland	+ 39.6	Jan	− 3.9	Q4	na	na	111.7§	114.2	0.81	0.77	1.45	–	0.69	− 0.9
Luxembourg	− 4.9	Jan	+ 3.6	Q4	na	na	106.4§	107.7	0.81	0.77	1.45	–	0.69	− 2.3
New Zealand	− 5.0	Feb	− 9.6	Q4	na	na	126.5	137.5	1.58	1.38	2.82	1.94	1.34	+ 5.3
Norway	+ 51.1	Mar	+ 49.5	Q4	na	na	112.5	107.3	6.33	6.25	11.3	7.80	5.37	+ 15.3
Portugal	− 22.9	Jan	− 16.6	Jan	na	na	105.1**	106.6	0.81	0.77	1.45	–	0.69	− 6.0

*Merchandise. Australia, Britain, France, Canada, Japan and United States imports fob, exports fob. All others cif/fob. †Bank of England except §IMF, February average. ‡OECD estimate.
**IMF, December average.

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The Economist commodity price index

Apr 20th 2006
From The Economist print edition

2000=100

	Apr 11th	Apr 18th*	% change on one month	% change on one year
Dollar index				
All items	162.5	166.7	+ 7.1	+24.7
Food	135.1	135.2	+ 1.2	+ 6.0
Industrials				
All	197.8	207.5	+12.6	+46.4
Nfa†	148.9	149.5	+ 2.0	+14.9
Metals	224.5	239.1	+16.8	+61.4
Sterling index				
All items	141.0	142.2	+ 5.3	+34.4
Euro index				
All items	123.9	125.5	+ 5.4	+32.3
Yen index				
All items	178.8	182.0	+ 7.7	+36.9
Gold				
$ per oz	599.30	616.25	+12.1	+42.5
West Texas Intermediate				
$ per barrel	68.90	71.25	+18.4	+36.3

*Provisional. †Non-food agriculturals.

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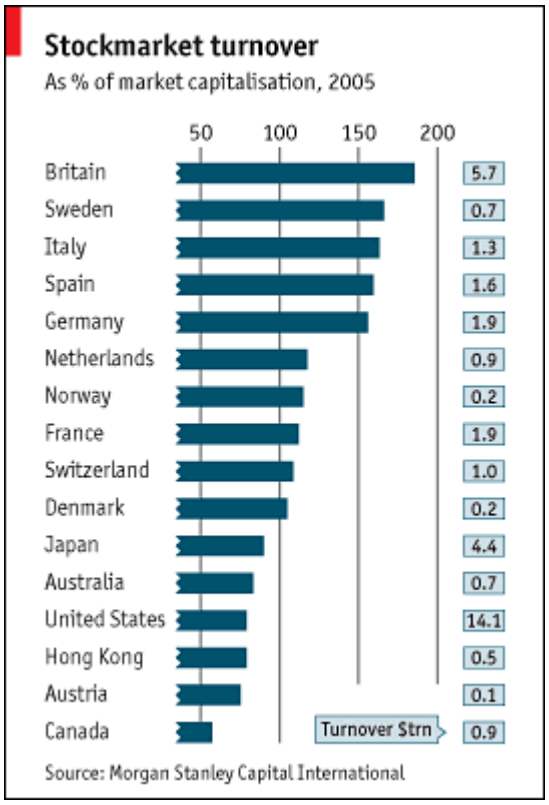
Stockmarket turnover

Apr 20th 2006
From The Economist print edition



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Overview

Apr 20th 2006
From The Economist print edition

China's GDP grew by 10.2% in the year to the first quarter, its fastest pace for ten years. Its foreign-exchange reserves rose to $875 billion in March, up by $216 billion from a year earlier. Thanks to higher oil prices, **Malaysia's** inflation rate rose to a seven-year high of 4.8% in the year to March.

Saudi Arabia's stockmarket has fallen by 25% over the past two weeks.

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GDP forecasts

Apr 20th 2006
From The Economist print edition

In 2006 all of the emerging economies that we track each week could enjoy faster GDP growth than America, Japan or the euro area, according to the IMF's latest forecasts. Even this year's laggards, Brazil and Mexico, are expected to grow by 3.5%. China is again tipped to be the fastest-expanding economy this year and next, with average growth of 9.3%, followed by India at 7.2%.

Economy

Apr 20th 2006
From The Economist print edition

	% change on year ago						Latest 12 months, $bn				Foreign reserves* $bn, latest	
	GDP		Industrial production		Consumer prices		Trade balance		Current account			
China	+10.2	Q1	+17.8	Mar	+ 0.8	Mar	+108.1	Mar	+128.5	H1	875.1	Mar
Hong Kong	+ 7.6	Q4	+ 5.9	Q4	+ 1.6	Feb	−11.3	Feb	+19.7	Q4	125.9	Mar
India	+ 7.6	Q4	+ 8.8	Feb	+ 5.0	Feb	−39.4	Mar	−13.3	Q4	145.1	Mar
Indonesia	+ 4.9	Q4	−17.5	Feb	+15.7	Mar	+29.8	Feb	+ 3.0	Q4	33.8	Feb
Malaysia	+ 5.2	Q4	+ 5.8	Feb	+ 4.8	Mar	+26.8	Feb	+19.9	Q4	71.6	Feb
Pakistan	+ 8.4	2005†	+19.3	Sep	+ 6.9	Mar	−10.5	Mar	− 3.7	Q4	9.8	Feb
Philippines	+ 6.1	Q4	− 2.8	Jan	+ 7.6	Mar	− 3.8	Jan	+ 2.4	Dec	18.0	Mar
Singapore	+ 9.1	Q1	+37.2	Feb	+ 1.2	Feb	+32.5	Mar	+33.2	Q4	122.2	Mar
South Korea	+ 5.3	Q4	+20.0	Feb	+ 2.0	Mar	+19.3	Mar	+11.1	Feb	217.3	Mar
Taiwan	+ 6.4	Q4	+14.1	Feb	+ 0.4	Mar	+ 8.9	Mar	+16.4	Q4	257.1	Mar
Thailand	+ 4.7	Q4	+12.8	Feb	+ 5.7	Mar	− 7.0	Feb	− 1.8	Feb	52.9	Feb
Argentina	+ 9.1	Q4	+ 3.7	Mar	+11.1	Mar	+11.3	Feb	+ 5.4	Q4	19.6	Feb
Brazil	+ 1.4	Q4	+ 5.4	Feb	+ 5.3	Mar	+45.8	Mar	+13.5	Feb	59.2	Mar
Chile	+ 5.8	Q4	+ 5.0	Feb	+ 4.0	Mar	+11.6	Mar	+ 0.7	Q4	16.0	Mar
Colombia	+ 3.7	Q4	+ 5.9	Jan	+ 4.1	Mar	+ 1.4	Jan	− 1.9	Q4	15.0	Mar
Mexico	+ 2.7	Q4	+ 5.4	Feb	+ 3.4	Mar	− 4.9	Feb	− 5.7	Q4	75.6	Feb
Peru	+ 4.9	Feb	+ 3.6	Feb	+ 2.5	Mar	+ 5.2	Feb	+ 1.0	Q4	13.4	Mar
Venezuela	+10.2	Q4	+13.6	Jan	+12.1	Mar	+31.5	Q4	+25.4	Q4	21.8	Jan
Egypt	+ 5.2	Q1§	+ 4.0	2005†	+ 4.0	Feb	−11.1	Q4	+ 2.2	Q4	21.3	Feb
Israel	+ 4.8	Q4	+ 8.4	Jan	+ 3.6	Mar	− 8.7	Feb	+ 2.4	Q4	28.0	Mar
Saudi Arabia	+ 6.5	2005‡	na		+ 1.5	Jan	+84.6	2004	+51.9	2004	23.2	Feb
South Africa	+ 4.5	Q4	+ 3.8	Feb	+ 3.9	Feb	− 4.7	Feb	−10.1	Q4	20.6	Mar
Czech Republic	+ 6.9	Q4	+11.8	Feb	+ 2.8	Mar	+ 1.7	Feb	− 2.6	Q4	29.4	Feb
Hungary	+ 4.3	Q4	+11.6	Feb	+ 2.3	Mar	− 3.3	Feb	− 8.0	Q4	21.5	Mar
Poland	+ 4.2	Q4	+10.1	Feb	+ 0.4	Mar	− 2.6	Feb	− 4.0	Feb	43.7	Feb
Russia	+ 7.0	Q4	+ 4.1	Mar	+10.6	Mar	+128.1	Feb	+84.3	Q1	205.9	Mar
Turkey	+ 9.5	Q4	+ 5.0	Feb	+ 8.2	Mar	−45.3	Feb	−24.7	Feb	56.5	Feb
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*											
Estonia	+11.1	Q4	+ 5.2	Feb	+ 4.0	Mar	− 2.6	Jan	− 1.5	Feb	1.9	Feb
Latvia	+10.5	Q4	+ 7.6	Feb	+ 6.5	Mar	− 3.0	Jan	− 2.0	Jan	2.4	Feb
Lithuania	+ 8.8	Q4	na		+ 3.1	Mar	− 3.8	Feb	− 1.8	Feb	4.2	Feb
Slovakia	+ 7.6	Q4	+ 5.5	Feb	+ 4.5	Mar	− 2.9	Feb	− 4.0	Dec	15.1	Jan
Slovenia	+ 5.1	Q4	+ 6.6	Jan	+ 1.9	Mar	− 1.7	Feb	− 0.3	Feb	8.5	Jan

*Excluding gold, except Singapore and China; IMF definition. †Year ending June. ‡Economist Intelligence Unit estimate. §2005.

Sources: National statistics offices, central banks and stock exchanges; Thomson Datastream; Reuters; WM/Reuters; Hong Kong Monetary Authority; Centre for Monitoring Indian Economy; Bank Leumi le-Israel; Standard Bank Group

Financial markets

Apr 20th 2006
From The Economist print edition

	Currency units			Interest rates	Stockmarkets	% change on		
	per $		per £	short-term	Apr 19th		Dec 30th 2005	
	Apr 19th	year ago	Apr 19th	% a year		one week	in local currency	in $ terms
China	8.01	8.28	14.3	2.10	1,464.6	+2.7	+ 20.0	+ 20.8
Hong Kong	7.75	7.80	13.9	4.65	16,830.4	+3.2	+ 13.1	+ 13.1
India	45.0	43.7	80.5	5.47	11,896.0	+4.8	+ 26.6	+ 26.6
Indonesia	8,905	9,585	15,930	13.46	1,453.2	+5.9	+ 25.0	+ 38.1
Malaysia	3.66	3.80	6.55	3.51	946.0	+0.4	+ 5.1	+ 8.5
Pakistan	60.0	59.4	107	9.30	12,048.1	+0.5	+ 26.1	+ 25.7
Philippines	51.4	54.4	91.9	7.63	2,223.7	nil	+ 6.1	+ 9.5
Singapore	1.60	1.65	2.86	3.38	2,585.8	+1.6	+ 10.2	+ 14.6
South Korea	946	1,011	1,691	4.36	1,437.8	+3.9	+ 4.2	+ 11.4
Taiwan	32.4	31.5	58.0	1.70	7,038.8	+3.4	+ 7.5	+ 9.0
Thailand	37.8	39.4	67.6	5.20	764.2	+1.2	+ 7.1	+ 16.1
Argentina	3.07	2.90	5.49	10.06	1,912.9	+3.4	+ 23.9	+ 22.3
Brazil	2.12	2.55	3.78	16.45	39,937.0	+3.9	+ 19.4	+ 31.8
Chile	514	577	919	4.80	9,922.7	+1.0	+ 7.8	+ 7.4
Colombia	2,345	2,343	4,196	5.88	10,898.0	−0.6	+ 14.6	+ 11.7
Mexico	11.0	11.1	19.7	7.21	19,933.1	+3.2	+ 12.0	+ 8.4
Peru	3.31	3.26	5.92	4.23	6,804.2	+5.2	+ 41.7	+ 46.9
Venezuela	2,515§	2,750§	4,498	10.59	30,951.5	−1.1	+ 51.8	+ 56.1
Egypt	5.75	5.80	10.29	8.56	55,346.8	−7.4	nil	− 0.2
Israel	4.55	4.37	8.15	5.28	869.9	nil	+ 5.1	+ 6.2
Saudi Arabia	3.75	3.75	6.71	5.02	13,261.9	−15.5	− 20.6	− 20.7
South Africa	6.00	6.13	10.7	7.15	21,100.6	+1.8	+ 16.6	+ 23.3
Czech Republic	23.1	23.1	41.4	2.10	1,533.8	+1.1	+ 4.1	+ 10.8
Hungary	216	190	386	6.28	24,434.1	+1.9	+ 17.6	+ 16.7
Poland	3.17	3.18	5.67	4.12	42,715.5	+2.2	+ 20.0	+ 23.3
Russia	27.5	27.7	49.2	12.00	1,615.0‡	+3.4	+ 37.3	+ 43.5
Turkey	1.33	1.36	2.38	14.14	43,732.5	+2.9	+ 9.9	+ 11.6
EM (MSCI)*	1.00	1.00	1.79	na	838.2	+4.3	+ 18.7	+ 18.7
EMBI+†	1.00	1.00	1.79	na	373.4	+0.6	+ 1.3	+ 1.3

*Emerging Mkts. †JPMorgan Chase's Emerging Mkts Bond Index Plus. ‡In $ terms. §Floating exchange rate.

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